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Foreword

This volume brings together the results of research and analysis conducted by the World Trade Issues Working Group from late 1999 through 2000, under the overall aegis of the Global Challenges and Opportunities Network (GCON). GCON had been launched as part of a larger policy research initiative (PRI) to advance the general objective of enhancing policy research capacity within the Government of Canada. Given the pervasive impact on national policies of globalization and trade liberalization, a key area for research centred on issues raised by Canada's participation in the global trading system.

As it happened, the timing of this initiative was fortuitous: the failure to launch a new round of multilateral trade negotiations at the World Trade Organization (WTO) Ministerial meeting in Seattle in December 1999 laid bare a number of fault lines and raised a spate of issues concerning the future direction of global trade policy. The World Trade Issues Working Group tackled these issues through a series of seminars with invited trade policy experts and research papers. The results have deepened understanding of the issues within the government; it is hoped through this compilation to make this work more widely available.

The papers compiled in this volume are very much in the spirit that the PRI envisaged when it launched the GCON working group process. The papers were for the most part written in the personal capacity of staff members from a wide range of participating departments; and they resulted in horizontal, cross-cutting analysis of challenging policy issues confronting the Government of Canada as a whole, while at the same time helping to rebuild the research capacity of the various participating departments. The interdepartmental collaboration created a new network of researchers, helping to break down the "stovepipe" approaches that are widely recognized as inadequate in addressing the complex interdisciplinary issues now facing public governance.

Particular credit for stimulating and leading this effort is due to the Chair of the World Trade Issues Working Group, John Curtis, Senior Advisor and Co-ordinator, Trade and Economic Policy, at the Department of Foreign Affairs and International Trade (DFAIT). John leveraged this output through a shoestring base budget, augmented by contributions elicited through a tireless "rainmaking" campaign within and outside DFAIT, and ensured that the work received prominent attention both at a featured workshop at the National Policy Conference in December 2000 and through the present publication. He oversaw the editing of this publication and also found time to contribute an original article.

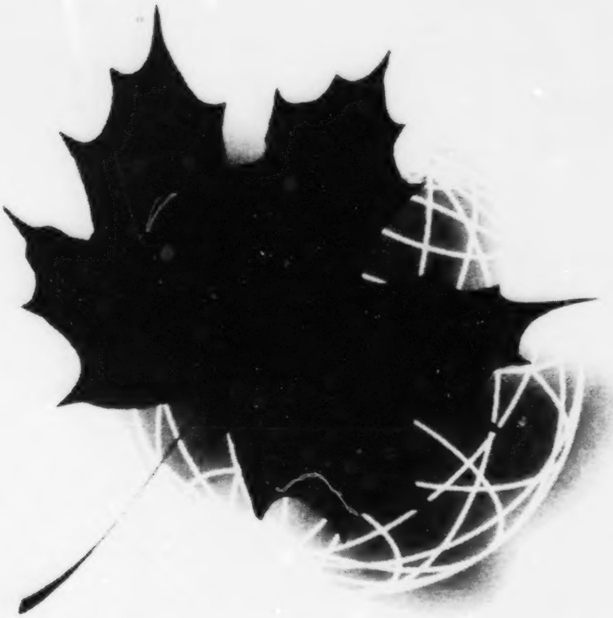
Also deserving particular recognition are the authors who volunteered their time and energy to develop the articles that comprise this volume: Dan Ciuriak of DFAIT, Bruce Jamieson of the Department of Canadian Heritage, Philippe Massé of Human Resources Development Canada, Kerry David Max of the Canadian International Development Agency, Robert Stranks of DFAIT and subsequently Environment Canada, and Jake Vellinga of Health Canada. Equally, thanks are due to Professor Jagdish Baghwati of Columbia University and Gary Hufbauer of the Institute for International Economics, who graciously accepted invitations to lead seminars with the World Trade Issues Working Group and to have summaries of their remarks included in the present volume. And, of course, thanks are due to the many participants at World Trade Issues Working Group seminars, from both within and outside the Government of Canada, whose insights contributed to the development of the ideas articulated in the various articles.

Finally, I would be remiss not to mention the organizational support to the Working Group from Sushma Barewal, Vicky Edgecombe, Brigitte Diogo, and particularly Christine O'Connell; their efforts ultimately made this volume possible.

Hugh Stephens
Assistant Deputy Minister
Communications, Culture and Policy Planning, DFAIT
December 2000

Part I

Reflections on Trade Policy Post-Seattle



Trade and Coherence: A Roundtable Discussion

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This note reports on a roundtable discussion of the complex set of issues under the rubric of "trade and coherence" held at the Department of Foreign Affairs and International Trade on January 21, 2000. Participants included invited experts on the global trading system, as well as the trade policy community within the Government of Canada. Following Chatham House rules, the views expressed at the conference are presented without attribution to individual participants. The usual disclaimer also applies: the remarks below are not to be attributed to the Department of Foreign Affairs and International Trade or to the Government of Canada.

The Context

In the wake of Seattle...

The causes and consequences of the failure of the World Trade Organization (WTO) Ministerial at Seattle in December 1999 to launch a new round of multilateral trade negotiations were not central themes for the roundtable but did not pass without comment. The outcome of Seattle obviously shaped the context for the discussions. As well, it necessarily serves as the point of departure for all considerations of next steps in process terms; ipso facto it determines the pace and modalities of progress on international trade and investment issues in the near term.

Moreover, the lessons learned from Seattle concerning the WTO (including its organization, capacities, procedures and interfaces with member governments, other international organizations, civil society and the general public) constitute important inputs to consideration of the various aspects of institutional and policy coherence in the world of trade. However, even if the Ministerial had not failed, the issues facing the international trade policy community would still be essentially the same – whether in the full glare of the public spotlight as currently or papered over through "constructive ambiguity" in the drafting of the communiqué and decision documents.

The exegesis of the causes of the failure ("whodunit") focusses on catalysts and accidental factors – the difficulties and delays from logistics; the long absence of executive leadership in the WTO during the preparatory process, which contributed to a poor starting point; the organized opposition from a broad swath of civil society organizations (CSOs); the disastrous atmospherics emerging from the media coverage; the absence of visible support from the business community (not to mention from CSOs whose concerns with development might have been thought to translate into support for new negotiations that were shaping up as a "development round"); the "bureaucratic" nature of the agenda, which may have explained the lack of interest of the business community;[1] and the many complications for the United States as host (which included the timing of the meeting vis-à-vis the domestic electoral cycle, the absence of fast-track authority, and so forth). In this context, the more fundamental difficulties proved impossible to overcome: these difficulties included the unhappiness of the developing countries with the negotiating process as well as the lack of evident benefits to them from the Uruguay Round; and the deep divides amongst the Quad partners (the United States, the European Union, Japan and Canada) and their preparedness to accept a failure rather than budge on key issues).

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[1] The "bureaucratic" label is not meant to impugn the importance of the issues to the longer-term health of the trade system. Rather, it is meant to contrast the slow, institution-building nature of these issues, and the long gestation periods for development and implementation of solutions, with the rapid pace of change in the modern business environment, which does not allow corporations to wait for the working out of issues in the fullness of time and thus leads them to find other ways to achieve their ends – as indeed is attested by the rapid expansion of trade and investment notwithstanding the turmoil in the rule-making area.

... unintended consequences of the Uruguay Round loom large...

A deeper understanding of the issues confronting the trade community today requires a look back to the Uruguay Round and some of its unintended consequences. In some views, what emerged from Marrakech was not so much the creation of the framework for a world trade system as the more or less wholly unprepared launching of a project for a single global economy. This pivotal – and unintended – shift was marked by the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), the incorporation of which into the WTO framework opened a Pandora's box of issues for the trade system.

Under the General Agreement on Tariffs and Trade (GATT), an implicit buffer had existed between international and domestic policy space – international regulations might constrain actions of governments but did not dictate the content of domestic rules. TRIPS, by setting out specific requirements for domestic regulation, breached this buffer.

Second, TRIPS established a precedent for using the trade system to deal with non-trade issues that were being addressed less than satisfactorily elsewhere. In the case of intellectual property, the inability of the competent body, the World Intellectual Property Organization (WIPO), to adequately enforce intellectual property rights at a time when trade in knowledge-based products was growing by leaps and bounds led to pressure (mostly from U.S. business) to deal with the problem through the trade system.

Third, the actual contents of the intellectual property rights agreement were negotiated within the trading regime's rule-making system. The embedding in the global economic system of certain values (specific rights for intellectual property) in this manner opened the way for pressure for similar embedding of other values – human rights, environmental safeguards, minimum labour standards and so forth – issues that had been dealt with in the international domain principally and for the most part ineffectually through hortatory agreements under the United Nations and other agencies.

In a similar vein, a view was put forward that TRIPS was not the only source of new complexities opened up by the Uruguay Round: pursuant to a mandate in the Marrakech agreement, the subsequently concluded Financial Services Agreement introduced, it was argued, the precautionary principle into the legal framework of the WTO. This opened the way for its application in areas where there were realistic hopes for science-based checks and balances, but also in areas where such hopes were slim given inherent longer-term uncertainties (e.g. genetic modification) and in areas where no such hopes existed at all (e.g. culture).

Management of the sorts of issues and tensions encountered when striking balances between different values and acceptable levels of risk is difficult enough at the nation-state level. Complicating matters hugely for the project launched by the Uruguay Round was that, due to success in bringing developing economies into the rules-based system, the single global economy was to emerge from a group of nation-states that differed enormously in their domestic regulatory structures. Some, principally in the Organization for Economic Co-operation and Development (OECD), were in the midst of the Thatcher-Reagan revolution, whose objective was characterized as the "withering away of the economic regulatory state." At the same time, these same states were refining complex social regulatory frameworks developed to, first, sustain long-standing social compacts that temper the distributional effects and social impacts of giving fuller rein to market forces; and, more generally, to manage the technical/scientific, ethical and cultural/political issues of a technologically advanced society.[2] Other states, mostly outside the OECD, were not only resisting economic deregulation but were not embracing social regulation. Indeed, for the most part they lacked social compacts, not to mention the governance frameworks, technical capacity and domestic economic and political incentives needed to create and effectively implement such a regime.[3]

...and the WTO must deal with the problems that have grown out of its successes

The WTO that emerged from the Uruguay Round to guide and nurture the evolution of the single global economy had a much larger membership than the GATT (since grown to 135, with a list of 30-odd applicants waiting in line) and faced a widespread desire to resolve issues in other areas through WTO mechanisms. Although these are problems of success and not of failure, in the view of some, the challenges they posed overmatched the minimalist and legalistic structure of the WTO and its resources.

First, the accession of a large number of developing countries to the WTO extended trade rules to the clientele of the World Bank at a time when, based on the lessons from the "Asian Miracle" (which had firmly established that trade and investment were key engines of economic development) the World Bank was making trade and investment central planks of its development programs – and in effect was becoming a trade facilitation body.

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[2] Between the 1960s and the 1990s, social regulation in the OECD experienced an "inflation" of 300-400 percent. While some bemoan this, as the connotations of the term "inflation" suggest they might, others see it as necessary, in that as the domain of the market expands so does the state's welfare role.

[3] New entrants (China, Russia, et al.) will not simplify matters in this respect – rather the converse.

Second, by 1999, as a result of the growth of foreign direct investment, sales of foreign affiliates surpassed the volume of cross-border trade, making the latter mode, for the first time, the junior partner in international commerce. In this context, distinctions between trade policy and broader economic policy (i.e. investment rules, subsidies, competition policy, etc.) become murky, if not totally collapsed (as they are in the case of trade in services); moreover, the institutional contest over trade rules takes on new life. And then along comes electronic commerce...

Third, the sheer growth in trade in relation to overall economic activity had qualitatively changed matters. At one time, trade accounted for about 7 percent of global production; in effect this represented the exchange between essentially *independent* economies of relatively small (percentage-wise) quantities of excess national production. Now, when trade accounts for about 25 percent of global production, it occurs between *interdependent* economies. Trade issues accordingly move from the periphery to the centre of overall economic policy and thus to the domain of institutions such as the International Monetary Fund (IMF) when problems arise, and more generally to domestic economic policy agencies, where trade disciplines are liable to be viewed as infringing on sovereignty.

The Issues: Institutional Aspects of the Trade and Coherence Agenda

What governing structure does the global market require?

The present systemic requirements clearly go beyond adding a few "bells and whistles" to the GATT/WTO system. However, the answer from Seattle to the question of what changes should be made to the global governance structure was essentially "we don't know yet." Absent a consensus on a grand plan, and attention then returns to practical problems.

The trade system may be unsustainable if it does not address labour, environment and human rights; at the same time, the trade system cannot do the "heavy lifting" on these most difficult issues.

A warning sounded by UN Secretary-General Kofi Annan a year before Seattle concerning the risks to the sustainability of the trade system if it did not somehow address the labour, environment and human rights issues apparently had some prophetic force. While the reaction against trade and the desire to "piggyback" the "values" issues on the WTO might seem mutually contradictory impulses, they can be reconciled: their common root cause is the lack of effective action on the values issues in the face of effective management of trade issues. It was suggested that the pressure to use the trade system to deliver results in these other areas will be harder to resist because of TRIPS – if the WTO can negotiate and enforce intellectual property rights, why can it not help enforce the Montreal Protocol in the case of the environment, or labour rights on behalf of the International Labour Organization (ILO)? The options for doing this would range from simply extending a blanket waiver for trade retaliation (as can be done for violation of internationally agreed standards), to bringing agreed standards into the WTO, to actually negotiating the standards, as was done in the case of TRIPS.

To some this is an alarming trend as it threatens to overwhelm the WTO, which is in difficult straits following a protracted period without leadership and an ill-prepared and ultimately failed Ministerial, in disarray over procedures (reform of the "green room" process, involvement of CSOs), and facing expectations in terms of analytical work, consultation and co-ordination, capacity-building assistance and surveillance well beyond its resources.

One logical framework that suggests itself is a partnership between the WTO and other institutions involved in regulation of international commerce, including the UN in cases such as the law of the sea, civil aviation authorities, the International Telecommunications Union, the ILO and so forth. Strengthening the partnership between the WTO and the UN was in fact suggested by WTO Director-General Mike Moore in a presentation to the UN on January 19, 2000. Such a relationship would recall the historical ties between the WTO and standards-setting organizations; to the extent that the UN could broker a consensus, it would not be difficult for the WTO to recognize it. Similarly, the WTO could benefit from the resources and knowledge of the IMF and World Bank in its surveillance function[4] (although the spectre of the cross-conditionality to which this might lead creates considerable nervousness in many countries – notwithstanding the limitations placed on cross-conditionality at Marrakech). If one thinks of the WTO's functions as divided into "hard law" (e.g. administering dispute settlement, TRIPS, etc.), "soft law" (procedures, implementation, etc.), capacity building and surveillance, this approach would have the WTO concentrate heavily on the first role while looking elsewhere for support for the other roles.

A second way forward is the Global Compact being advanced by the UN; this initiative is attempting to opportunistically take advantage of the pressures on the business community to respond to the "values" issues in a spirit of voluntarism.[5]

Fortunately, the "hard economics" do not necessarily pose obstacles to progress in reconciling labour and environmental issues with trade. As was in a sense rediscovered in the course of the Asian Crisis, addressing labour issues (e.g. through training and provision of social safety nets) assists in curtailing the decline of demand during downturns, helping to stabilize economies. In a similar vein, the higher incomes generated by economic growth generate demand for a cleaner environment as well as the wherewithal to achieve it. The question really is how to initiate these virtuous circles.

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[4] This is very much in the spirit of the Integrated Framework, although the implementation of the latter has left something to be desired. For example, the World Bank supports programs for customs, but not necessarily the aspects that would be of interest or value to the WTO (e.g. in customs valuation).

[5] The notion promoted by Jagdish Baghwati of "behave abroad as you do at home" envisages actors with established "economic rights" sharing the burden of development in these areas. Much regulation (typically of a positive nature) is in any event private sector driven; the state usually enters to introduce the negative, "thou shalt not" type of regulations, often in cases where the precautionary principle would apply. The OECD is currently preparing a survey of the extent of self-developed standards in the private sector. While this is promising, it was argued that it will be important that a strong base of homework be done before the issues are brought to the WTO.

Is institutional coherence – in the sense of negotiated clarity as to roles and responsibilities – a realistic proposition?

Much has been made of the written agreement between the IMF and the World Bank as an example of how to generate institutional coherence amongst the international institutions. However, in its practical application, this agreement was described as being less a means of co-ordination or harmonization of policies than a minimal check on working at cross-purposes. Effective burden sharing is less a question of formal agreements on paper than a sense of ownership of the issues by the institutions involved.

Indeed, this reflects a more general feature of societies, which function largely on the basis of protocols that are not written down but understood and accepted.[6] Attempts to write these protocols down would be counterproductive, if at all possible. Accordingly, negotiated clarity as to which international institution does what with which clients in which circumstances is simply not realistic, especially since the set of "trade and..." issues is turning out to be much larger and more complex than was previously thought.

One metaphor that has been suggested to capture this sense of "bottom up" order – order generated not through centralism but rather pluralism[7] – as the basis of essential coherence is "rhythm"

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[6] The notion that post-Westphalian nation-states function largely on the basis of formally developed rules is to some extent a myth; shared values and unwritten rules play a large role.

[7] This concept contemplates the citizen's – and by extension, the CSOs' – participation in national life above and beyond the act of voting in elections.

(a sense of being in step with the times, alert to developments and opportunistically prepared to engage co-operatively but with no more overt co-ordination than occurs, say, amongst couples on a dance floor or in a jazz band in full improvisational flight).[8] A practical example in the trade policy area might be to involve organizations and groups such as the ILO, the World Wildlife Federation and cultural associations in a country's Trade Policy Review Mechanism (TPRM) reviews, allowing them to comment on a country's policies, progress on implementation of trade-related commitments in their areas of concern, and so forth.

The Issues: Policy Aspects of the Trade and Coherence Agenda

Trade and development: shifting from "putting development into trade" to putting trade into development...

The "old formula" of putting development into trade through special and differential (S&D) measures has not only created a mess in the WTO, it was argued, but has failed in its purpose. It has not worked well for the developing countries, and such benefits as it delivered are eroding over time as the value of preferences falls with the general decline in tariffs worldwide. This experience, coupled with the success of trade-led development in East Asia, has led to a shift in thinking to emphasize trade

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This, it was argued, is the sound basis for CSOs' participation in international forums, rather than the notion that they represent interests or values. At the same time, clarity is needed concerning roles (e.g. CSOs can participate in the discussions but, in governmental forums, the governments decide), and questions need to be addressed concerning advocacy by CSOs. As a historical footnote, such participation is also far from new: as was pointed out, CSOs were involved in the League of Nations.

[8] This concept is developed in Robert Wolfe, "Rendering unto Caesar: How Legal Pluralism and Regime Theory Help in Understanding 'Multiple Centres of Power.'"

facilitation as part of development policy (e.g. in the Comprehensive Development Framework and the Poverty Reduction program).

Trade and finance: the WTO is prepared to liberalize financial services, but the IMF emphasizes prudential regulation...

The WTO is ready to proceed with financial services liberalization; the technical support is in fact in place. However, the institutional and policy interface issues raise significant difficulties. The financial services agreement in the WTO was made possible only by carving out the supervisory aspects; the IMF now wants to ensure that financial liberalization proceeds only in the context of adequate supervision and regulation ("proper sequencing" is the phrase of finance ministers), a response to the view that the Asian Crisis was due to liberalization of financial markets in a context of inadequate regulatory and supervisory systems. Moreover, there is a structural issue given that a country can renege on commitments under the General Agreement on Trade in Services (GATS) for two reasons: balance of payments difficulties or at the request of the IMF.

Trade and investment

The growth of foreign investment and the absence of business support for the Multilateral Agreement on Investment (MAI) beg the question: where is the market failure that creates the need for a multilateral instrument on investment? Perhaps, indeed, there is no market failure – firms are finding a way to deal with the issues that affect them.[9] Moreover, the GATS is an effective instrument for liberalizing services trade, which is where investment liberalization really matters.

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[9] Indeed, given the fact that business can use regulatory arbitrage to obtain favourable conditions for investment, not to mention the length of time it takes to negotiate and implement an agreement compared to the time horizons in which business decisions are made, it is an open question why business would ever support a multilateral instrument that would minimize the scope for such

Nonetheless, concerns about the functioning of the system might lead one to conclude that the present messy patchwork quilt of bilateral Foreign Investment Protection Agreements (FIPAs), etc., needs to be replaced by a sound multilateral framework – if only to lock in the current comparatively liberal regime for global investment. In this case, the big challenge will be to address services.[10] Since states do not necessarily want to be constrained in competing for direct investment (or policy freedom more generally),[11] consideration would also have to be given to the content of a multilateral investment agreement. As well, what would the "architecture" be? For example, could a "variable geometry" regime work (as in the case of the Telecommunications Agreement, where the "critical mass" approach worked and did not undermine the single undertaking)?

Given that multinationals tend to look at their operations in regional terms, a second approach would be to consider developing regional investment frameworks. By levelling the playing field regionally, regional investment frameworks may be where the biggest "bang for the buck" will be.

A third consideration is dealing with the "demand" side of investment – addressing bribery and corruption. One might consider "migrating" the OECD guidelines on multinational corporations to Geneva. Extraterritoriality also remains an issue.

Trade and labour, environment, culture, etc.: a complex new world...

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arbitrage and not resolve any of the problems that it faces in the foreseeable future. At most, the small-business community might benefit.

[10] It can be noted in this regard that 91 percent of the NAFTA non-conforming measures are in services sectors.

[11] It was noted in this regard that economic policies such as Canada's National Energy Program would have been ruled out by an MAI.

The interface between the WTO and the regulation of international commerce more generally is not new. Indeed, at any given time, there are several *thousand* active committees under the International Organization for Standardization (ISO) alone, working on the technical nuts and bolts of the global economy. This activity is open to all states[12] and in many cases directly involves business (in some high-technology areas, such as telecommunications, the majority of the participants are corporate – and not simply in an advisory capacity, but as voting members), as well as civil society organizations (typically in an expert advisory capacity).[13] For the most part, this low-level activity has proved to be highly successful, and a well-established if informal protocol governs the relationship between the various actors: the international standards are set by the competent international organization and are recognized and deferred to by the WTO, with departures from international standards accepted to the extent that they are no more restrictive of trade than the internationally agreed norms. Nonetheless, when some of these issues get caught up in the trade system as technical barriers to trade (TBTs), jurisdictional issues are raised.

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[12] Developing countries would be hard-pressed to participate meaningfully. While in one sense this is not especially problematic, since the subject matter tends not to be relevant to them (strength of bolts on airplane wings, etc.), in another sense it does raise questions of buy-in, since the standards are thus effectively set by developed countries, reflecting developed-country norms, legal frameworks for liability and social attitudes concerning risk. At the same time, there really is no flexibility to lower the standards since they would then lose their purpose for developed countries. The complications as regards technical assistance for capacity building are clear.

[13] Some less successful examples include the now largely lapsed attempts to regulate commodity prices internationally through commodity organizations under the UN Conference on Trade and Development (UNCTAD); an echo of this is the continuation of some activity by the World Bank in managing the global commodity futures market.

As noted, the TRIPS agreement has opened up new possibilities for the WTO's role in the regulation of international commerce – if the WTO can negotiate and enforce intellectual property rights, why not the Montreal Protocol in the case of the environment, or labour rights on behalf of the ILO?[14] The options for the WTO would widen from simply extending a blanket waiver for retaliation (as can be done at present for violation of internationally agreed standards), to bringing agreed standards into the WTO (stating what can and cannot be done in the area), to actually negotiating the standards as in the case of TRIPS.[15]

One major complication looming over this whole range of issues is the precautionary principle: absent overwhelming scientific justification for standards, and issues turn on questions of consumer choice and different levels of risk aversion across societies – and in the case of culture, questions of what makes us "us." There have been some successes in handling this class of issues in the WTO – the French scallops case in the WTO provided an example of how to deal with the precautionary principle through voluntary labelling. However, in some views, given the potential for abuse,[16] the precautionary principle is a ticking time bomb[17] that urgently needs to be addressed – perhaps by redressing a glaring weakness in the international institutional framework from the failure of UNESCO to provide an authoritative voice on science and technology issues, as it originally was conceived to do. Probing this set of issues generally returns us to the issue of how to define the buffer zone between international and domestic policy – in the end there are legitimate questions of social choice (community involvement and the building of trust and credibility) that cannot, as it was put, "be resolved by appeal to unaccountable people in white lab coats."[18]

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[14] This leads some to contemplate throwing out the TRIPS agreement, and the GATS for good measure, in order to preserve the rest of the trade system.

[15] It was noted that the WTO text at Seattle would have resulted in holding to past practice (i.e. standards simply being recognized by the WTO).

[16] Credibility has already been strained by its application in circumstances that raise strong suspicions of cheating.

[17] Indeed, a time bomb that may already have gone off, as evidenced by the call for a World Council on Food Safety. The OECD is doing work on behalf of the G-7 on this issue, and the issue is receiving attention in environmental policy circles as well as elsewhere.

For the WTO, this might mean having to improve its interfaces with labour (ILO), environment (UN Environment Program, or UNEP) and health groups.

From a practical perspective, where is there scope for progress on trade issues?

For Canadian business, trade problems are principally seen as lying in the bilateral trading relationship with the United States, and this is where it was suggested that the government will find resonance for its initiatives. Nonetheless, there would be merit in promoting a deeper understanding within the business community of the extent to which it is the multilateral system and its rules that help make the NAFTA regime robust.

More generally, the regional front needs attention, at least in the Americas, where there has been little progress in the Free Trade Area of the Americas (FTAA) process on delivering the basic bargain made at Miami (market access for democratization). Moreover, this bargain is in fact becoming harder to fulfil given a steep rise in pressures on Latin American countries to live up to North American standards in terms of labour and the environment, while movement on the economic (market access) front has yet to materialize.

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[18] In fact, as in the case of the Charlottetown Accord, there are instances where all the experts agree but the public goes against the expert view.

One area where practical problems face the trade system today is frictions over processes and production methods (PPMs). Some of the most important work underway today is to address these problems through mutual recognition agreements (MRAs) that smooth the way for trade, without fanfare but in ways that matter very much to the business community. For business, therefore, the "new coherence" issue turns out to be the "old coherence" issue.

On standards, it was argued that the emphasis needs to shift from product specifications to performance specifications. At the same time, because performance specifications are looser, it is important that there be confidence in certification – hence the need for a competent international certification body presiding (which could directly involve CSOs, as in the case of forest products, where CSOs help set standards).

This of course does not gainsay the need for governments to address the longer-term governance issues facing the globally integrated economy – even if these issues, which for the most part revolve around points of bureaucratic conflict and therefore are of interest primarily to public officials, are ignored by the business community.[19] Many of these issues (e.g. improvements to the dispute settlement mechanism) do not require a "round" and could be addressed on an incremental basis.

That being said, some problems (e.g. agricultural subsidies) may defeat consensus, requiring a broader range of issues to be put on the table in order to provide the basis for trade-offs. In short, a round might be needed, although there is no agreement yet on what the shape of the next one would be.

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[19] Nor does it gainsay the desirability of greater engagement in this endeavour by those in the business community who have the ability (and the luxury) to look beyond the next quarterly profit statement.

Summary and Conclusions

First and foremost, Seattle was the not-unprecedented failure of a trade Ministerial, not of the trade system itself. There continues to be a rapid expansion in the exchange of goods and services internationally as well as in investment flows.

Second, the WTO faces major institutional challenges:

- it needs substantially strengthened resources;
- its internal structure needs to be reformed; in particular, the "green room" process needs to be replaced with a viable executive committee that is transparent, legitimate, negotiated and agreed; and
- a reasonable balance needs to be struck regarding which issues migrate into the WTO versus those that are kept at arm's length – a pure WTO is probably as unlikely to emerge as one that becomes a receptacle for every issue that comes along; the WTO's interfaces with other key international institutions (e.g. the ILO, UNEP, UNESCO and others) need to be developed accordingly; and consideration needs to be given to possible new institutions (e.g. a World Environmental Organization).

Third, recognizing that reforms to the WTO only scratch the surface of the problems, other institutions such as the World Bank have to shoulder some of the burden being placed on the WTO, especially in respect of "getting trade into development."

Fourth, there is a need to renegotiate the boundary or buffer between the international regulation and domestic policy space. How this might be done clearly deserves some considered thought.

What It Will Take to Get Developing Countries into a New Round of Multilateral Trade Negotiations

Jagdish Bhagwati
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This note summarizes comments on the set issues under the rubric of "trade and development" by Professor Jagdish Bhagwati of Columbia University at a seminar organized by the World Trade Issues Working Group at the Department of Foreign Affairs and International Trade in March 2000. The usual disclaimer applies: the views presented at the seminar and reported here are not to be attributed to the Department of Foreign Affairs and International Trade or to the Government of Canada.

The North-South divide that was fully exposed at the World Trade Organization (WTO) Ministerial meeting in Seattle in December 1999 was one of many factors that contributed to the failure to launch a new round of multilateral trade negotiations at that time. Since the world trade system works by consensus, the developing countries have to be brought onside in order to achieve the launch that ministers, trade officials and the WTO are actively working toward. The following are some key elements of a framework that would work for the developing countries.

Developing countries are now major players and must become full parties to the "give and take" of trade negotiations

The concept of different economic systems for developing versus developed countries (special and differential measures, in the parlance of trade policy) has essentially been discredited: it is now understood that there is a single economics for all. Institutional differences must be taken into account when applying this same economics; the developed countries, however, are looking for some reciprocity. By implication, developing countries will not get a "free lunch."

Indeed, one reason why the trade system has not worked all that well for developing countries (some countries have "graduated" while others have regressed) was that they never did have much of a free lunch. The system of consensus on a most favoured nation (MFN) basis works against those who make no concessions; thus the developing countries that offered little got little. For example, key markets such as textiles and agriculture remain subject to tight restrictions that are only now being incrementally eased as a consequence of the Uruguay Round.

It is essential that developing countries come to accept that their future participation in trade will depend on an exchange of mutual benefits – in other words, they must be fully part of the "give and take" of trade negotiations.

The expansion of trade rules in the Uruguay Round to include "inside the border" measures is perceived as a threat by developing countries. Their fears are amplified by the way in which non-governmental organizations and others in the developed countries, including some governments, have framed the issues

There is first a need to understand that this perception exists and that it needs to be addressed. The concept of general equilibrium shows that everything is eventually related to everything else. This is not very helpful, however, and some lines will have to be drawn as to what is trade and trade-related policy – and what is not. Several, if not many, of the issues that have been brought into the realm of trade policy issues are in fact broadly *trade-unrelated.* Continuing to deal with them in a trade context is damaging to the cause of getting developing countries to support a new round.

The Trade-Related Intellectual Property Rights (TRIPS) agreement concluded in the Uruguay Round was the first intrusive element and has had many, largely unanticipated, consequences. On the economics of the issue, while there is arguably some limited need for patent protection, the evidence does not show much of a supply-side effect on production from intellectual property rights protection.

Moreover, TRIPS does not involve mutual gain; rather, it positions the WTO primarily as a collector of intellectual property-related rents on behalf of multinational corporations (MNCs).[1] This is a bad image for the WTO and in the view of many, especially the non-governmental organizations (NGOs), reflects the "capture" of the WTO by the MNCs.

Several high-profile cases in recent years have entrenched this perception among NGOs and underpin their claim that the WTO should do the same for nature, human rights and other causes. At present, the General Agreement on Tariffs and Trade (GATT), General Agreement on Trade in Services (GATS) and TRIPS form a tripod within the WTO. But the tripod threatens to turn into a centipede as other issues are introduced. It is scarcely surprising, given the way that the NGOs frame these issues – the name of the game being to encourage the use of trade sanctions to advance their agendas – that they are perceived as threats by the developing countries, undermining for them the traditional perception of the WTO as a safeguard for the weak against the large players within the trade system.

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[1] This and other concerns emanating from the WTO's role in trade disputes have led some to consider the creation of a World Trade Court or to advocate shifting the Dispute Settlement Mechanism to the International Court.

In particular, labour and social issues need to be separated from trade sanctions – indeed, they need to be moved completely out of the trade picture. The United States and European Union pushed for a working party at the WTO Ministerial; however, while the U.S. was saying that this was "not a foot in the door," the developing countries saw it as "two feet in the door." President Clinton's statement that trade sanctions *were* in the picture had an electrifying effect on developing countries in Seattle.[2] To get developing countries into the trade round, children's/workers' issues, legitimate as they are, need to be clearly moved to the International Labour Organization (ILO), where they can be addressed without the threat of trade sanctions.[3]

Environmental issues are quite different from labour issues: all sorts of environmental issues are now being dealt with in the WTO; the developing countries need to engage on them

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[2] The U.S. action was highlighted on the day of the NGO meeting in Seattle. The 1930 Trade and Tariff Act was used to take this issue to the WTO; if it gets into the WTO and the WTO strikes down the U.S. action, it was argued that the NGOs will use this as ammunition to say that the WTO is pro child labour.

[3] Trying to get at the child labour issue in South Asia via trade is counterproductive – an OXFAM study in Bangladesh showed that a ban on child labour drove girls into prostitution. It was argued that the World Bank and International Monetary Fund should also remove themselves from these issues; indeed, even UNCTAD [UN Conference on Trade and Development] is difficult for developing countries because of the "T." The way to go is via ILO programs to get children into school. Apropos this issue, the fact that the United States is not signatory to many ILO conventions is not a sign of non-engagement, but simply a reflection of the fact that the U.S. does not sign on to promises that it cannot deliver on – unlike many countries that sign everything and can deliver little. One reason for this is the very complex institutional setting. The U.S. ratification process is very difficult and, moreover, there are private enforcement mechanisms in the U.S. not available in other countries.

For better or for worse, environment is well established in the WTO. The Dispute Settlement Mechanism is already pronouncing on the issues, and developing countries cannot afford to be on the sidelines. Of particular concern to the developing countries is that processes and production methods (PPMs), which experience has shown can be used for trade protection purposes,[4] have been addressed within the context of the Dispute Settlement Understanding (e.g. the shrimp-turtle decision), although it is an open question whether issues such as those surrounding PPMs should be negotiated rather than litigated within the WTO.

Having environment dealt with at the WTO raises many issues – in particular, the compatibility of trade rules and the environment accords needs to be sorted out. At a minimum, a grandfathering approach needs to be established. This is an argument to get developing countries into negotiations because they stand to lose if judges and other legal experts are left to decide the issues in the WTO.

Keep investment policy low-key and competition policy on the back burner

The effort to negotiate a Multilateral Agreement on Investment (MAI) in the OECD touched raw nerves; this is a good time to keep investment issues low-key. At the same time, some sense of stakeholder commitment is needed from multinational corporations; having no obligations on MNCs is inconsistent with where Western societies are heading.[5]

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[4] See, for example, the famous case of Swiss restrictions on German cheese, which were based on processing requirements but were transparently protectionist in intent. A description of the shrimp-turtle case may be found on the WTO website (http://www.wto.org/english/tratop_e/envir_e/edis00_e.htm).

[5] However, pushing for "living wages" is not a good way to go – this benefits those already with jobs in the developing countries, not those on the outside looking in.

This issue, and competition policy as well, is being pushed primarily by the European Commission without an apparent or clear political rationale.

Democratic deficit: transparency concerns need to be sorted out from the issue of representation

There are three elements to the concerns about the democratic deficit: negotiations, dispute settlement and everyday work. There is no problem with letting the world see what goes on in the WTO, including in the dispute settlement process. The WTO should open its doors, but NGO observer status and/or direct participation are false issues. The democratic deficit issues need to be sorted out because developing-country positions have hardened against NGO participation in negotiations following Seattle.

Implementation and an early package for developing countries are important to facilitate the process – but how it is done is just as important

The position of the International Monetary Fund/World Bank paper on trade and development – which proposes free market access for products from heavily indebted poor countries (HIPCs) – is problematic in that it risks simply shifting limited market access around amongst the poor rather than creating significant new market access for less-developed countries as a whole.[6] As usual, textiles are the key. As for trade-related technical assistance (TRTA), ultimately countries have to fend for themselves.

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[6] This is one aspect of a larger problem: trade is mutually beneficial provided it is non-coercive – this is true for the trading partners directly affected, but how about for third parties? Major initiatives such as the Uruguay Round have an impact on marginal countries, and that is where the international financial institutions should come in. The bananas case showed how an E.U.-U.S. dispute can affect mainly Caribbean countries, but the World Bank did not take a leadership role on their behalf.

If the developed countries are looking for appropriate signals, call the next negotiations a Development Round – and consider Delhi as the site to launch it.

Trade and culture

America is different. A key difficulty for the world community is the way the United States approaches culture and thus how to deal with the U.S. on this issue multilaterally. The United States does not see cultural imports as a threat; indeed it imports and absorbs culture from everywhere. Moreover, the U.S. is a "pill popping" culture – hence its relaxed view on genetically modified organisms (GMOs). By contrast, European fears of GMOs reflect cultural proclivities. Accepting that cultural diversity is a good thing, alternative ways need to be found to protect culture, since restrictions on market access will not work. Ultimately it is not desirable to dictate to consumers what they should see or read – subsidies, for example, can be used effectively.

Impact of Chinese accession to the WTO: entry of China will be good, and the WTO will be the "bull in the china shop"

China's accession will be beneficial from many perspectives. Not least, it will remove China from U.S. special considerations. As the U.S. actions on Russia's steel exports showed, the United States itself will benefit from having to play by the rules, in that this prevents arbitrary actions harmful to its own constituents.

But China will be hard to move (it is the proverbial 800-pound gorilla) and so progress will be slow even after accession. The point is to get it moving in the right direction. In this respect, the WTO could well be the "bull in the china shop" that helps move it down the right path. For the developed countries, the best policy otherwise might be described as the "open mouth" policy – be a "mosquito in the ear" that keeps putting the message incessantly.

Other issues

GATS safeguard mechanism: Acknowledging that a safeguard would facilitate entry into wider commitments by developing countries in the services area, it is difficult to think of a suitable mechanism – a standstill was one idea advanced. This issue was widely discussed in the Uruguay Round without resolution.

Agriculture and multifunctionality: It is hard to see how this argument can be considered consistent with free trade. There are alternative mechanisms to achieve stated goals.

Conclusions

The WTO needs to have a mix of policy, law, economics and political/diplomatic input to be successful. The transparency issue is real and the WTO needs to be forthcoming; NGO representation is not a real issue. Some issues, if included in the framework of trade negotiations, would be "poison pills" for the developing countries and as such would prevent the launch of a new round. Labour and social issues need to be dealt with in other forums. Investment and competition policy should be put on the back burner. Developing countries need to engage on trade and environment as it is currently playing out in the WTO. However, it is not clear that what is left on the table creates the basis for broad-based or comprehensive multilateral trade negotiations.

Trade and Coherence: Where the Major Gains Lie

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Institute for International Economics

This note summarizes the commentary by Gary Hufbauer, Senior Fellow at the Washington-based Institute for International Economics, on the evolution of thinking as to where the major gains in the trade and coherence debate lie, and where governments should be placing their priorities, at a seminar organized by the World Trade Issues Working Group at the Department of Foreign Affairs and International Trade in April 2000. The usual disclaimer applies: the views presented at the seminar and reported here are not to be attributed to the Department of Foreign Affairs and International Trade or to the Government of Canada.

The case for globalization is strong. Poor people benefit from growth, percentage point for percentage point, and trade is vital for growth.

No proposition in economics is indisputable, but one that comes close is the tight positive correlation between growth in trade and growth in GDP. At the same time, there is a strong positive relationship between growth in GDP and growth in incomes of the poorest. Income disparities between the richest and poorest countries have tended to widen. Nonetheless, the relationship is roughly one-to-one within countries (whether rich or poor) between the growth rate in the per capita incomes of the lowest quintile of the population and the overall GDP growth rate. The exhaustive work of David Dollar and his World Bank colleagues merits the attention of everyone interested in the inequality issue.

While the trade-growth link is strongly supported by numerous studies, the econometric evidence is less clear about whether capital flows cause stronger growth. Examining the uneven performance of economies around the world, a case can be made that financial depth (the size of the combined banking, insurance and securities sectors in an economy relative to GDP) is linked to good economic performance. I mention the work of Ross Levine, Joseph Francois, Wendy Dobson and Pierre Jacquet. Wendy Dobson and I are now doing some speculative calculations on the benefits of capital flows to emerging countries, as well as the costs of financial crises. I should note, however, that econometric work by UNCTAD is equivocal on the connection between foreign direct investment and economic growth – cause or effect?

Since 1980, there has been a massive growth in trade and substantial improvement in the welfare of the majority of the world's population, especially in East Asia where the most rapid growth in trade took place. This growth has benefited four billion of the six billion people on the planet. However, two billion people continue to live in extremely poor circumstances. The worst economic performance is associated with hyperinflation and political chaos.

Even successful countries must cope with severe internal tensions

The successful countries have given up trying to achieve income equality in the Fabian sense of funding massive programs for the lowest quintile by heavy taxes collected from the rich. Instead, they accept the trade-off between overall growth within a market economic framework and the fact that some people will become very rich indeed.

Nevertheless, technology-driven wealth is generating envy and backlash. In the past, wealth was largely created by thrift, hard work and commanding leadership – puritan virtues. Today, wealth is created by brilliance. This is a big difference. Although the causal links between great wealth and globalization are hazy, a good part of the backlash is directed at the global economy and international institutions.

Even in the successful countries, there remains a strong public yearning for rough equality in health care. But technology-driven health care improvements are driving a significant wedge between the health care available to the rich and the care available to the poor or even the middle class. The widening of disparities of income and wealth in the era of information technology has been grudgingly tolerated by most market societies; widening disparities in health care may be accepted less easily. Coupled with ageing in all the industrial countries, the new health technology promises astounding increases in public budgets. It remains to be seen how this force affects the debate on globalization.

Meanwhile, the international institutions are losing public support

The basis of support for the international institutions is eroding due to the "democratic deficit." "Y'all come" rhetoric that aims to co-opt civil society organizations (CSOs) by involving them in the work of the international institutions is not working. The World Bank made the greatest effort in this direction and was the most heavily attacked in the April 2000 demonstrations in Washington.

Moreover, the co-option strategy is questionable because there is a severe problem of choice concerning the CSOs. Which ones speak for the public? At the national level, there are well-established processes for engaging civil society in developing policy (at the same time, it is notable that governments do not permit CSOs or other lobbyists into Cabinet meetings or give them a vote on legislation).

One possible way to address the democratic deficit problem is to involve parliamentarians, selected from appropriate parliamentary committees, in the international institutions. These men and women have gained legitimacy by standing for election and are involved in the issues. They could play a greater "oversight" role in the work of the international institutions. Perhaps the OECD could serve as the initial vehicle for trying this idea out.

In the current environment, there is a premium on practical versus visionary work and on narrowing the focus of the international institutions that have wandered afield from their mandates.

The World Trade Organization

The WTO is about trade: liberalization, safeguards, and the various administrative and legal instruments, including most importantly the Dispute Settlement Understanding (DSU). The WTO is broadly effective, notwithstanding the fact that some issues (such as the controversy over genetically modified organisms) will likely prove too large to be handled through the DSU. It is important that the WTO focus on trade. Recalling the percentage-point-for-percentage-point gains in income for the poor from trade-led growth, bringing down market access barriers in developed countries is a priority.

Two issues that some are urging be introduced into the WTO are "poison pills": environment and labour. In the Uruguay Round, the WTO probably went too far in incorporating intellectual property rights (particularly in the case of pharmaceuticals) into the core of the trade regime. The TRIPS agreement continues to elicit an adverse reaction from developing countries. Moreover, it paved the way for CSOs in industrial countries to urge that environment and labour concerns be added to the WTO agenda. These issues need to be addressed in a different manner.

Labour issues, for example, need to be handled through the International Labour Organization (ILO). The ILO is in a revival phase. It has enforcement mechanisms in its articles, although these have never been used. They could be used to advance the agenda on "core" labour standards. Other mechanisms could be developed or used in this connection:

- Civil sanctions are available in some countries.

- The ILO could "rate" the regulatory framework for labour standards.
- A labelling system could be developed that would allow consumers to distinguish between products in terms of the labour conditions under which they were produced. Firms that have better working conditions could cite their adherence and increase their market share.

By contrast, environmental institutions are weak and operate in a fragmented framework. There are few truly global environmental issues; in fact, at present there may be only two: ozone protection and global warming. Most issues are largely national in scope – rain forests, endangered species, waste disposal, and so forth. In the environmental area, we need imaginative thinking on ways to advance the agenda that do not entail trade sanctions. Some of the approaches I have outlined for labour standards may be applicable in the environmental realm.

There are two other emerging issues facing the international economy that may involve the WTO: e-commerce and competition policy. The WTO could attack the thick underbrush of issues (taxes, customs procedures, etc.) that need to be cleared away to allow e-commerce to develop efficiently. The recent wave of cross-border mega-mergers raises troubling questions. What are their long-term competitive implications? The starting step might be a United States-European Union agreement to establish a basis both for approving future mega-mergers and for monitoring the market outcomes.

The World Bank

Of the international institutions, the World Bank has been the worst offender in terms of wandering far afield from its mandate. While it has a good image (testimony to effective public relations work by its leadership), it is organizationally a disaster (with layer upon layer of management). It tries to do too much for too wide a range of countries.

The World Bank needs a major shift of emphasis. In middle-income countries, it needs to concentrate on the bottom

20 percent of the population. For the 1.5 billion people living in chaotic nations, the World Bank needs to build the civil conditions that are the prerequisite for economic growth. Typically, disasters arise following the seizure of power by a small group that subsequently pillages the economy. Re-establishing the basis for growth requires wholesale administrative change. The World Bank could work with donor countries to provide, on invitation by countries emerging from civil chaos, a cadre of administrators who would build the institutions necessary for effective markets – a judiciary, stock market and so forth. Basically, this prescription amounts to receivership for countries in the worst straits, nations such as Congo and Sierra Leone.

The International Monetary Fund

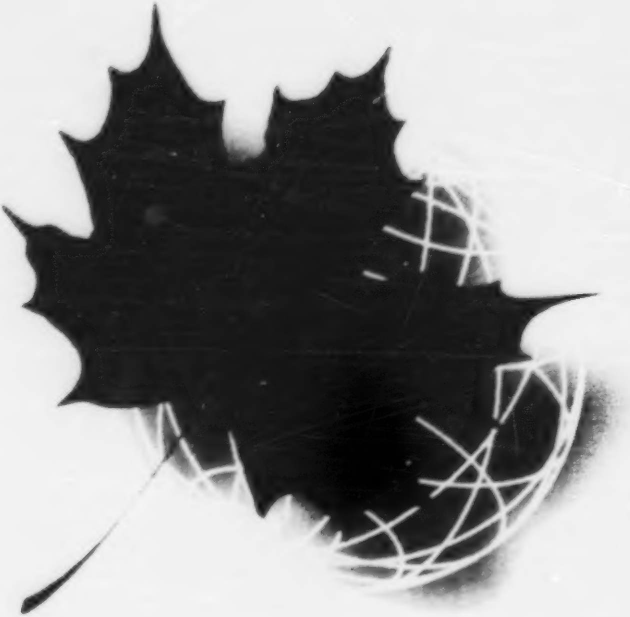
The call by the recently retired IMF managing director, Michel Camdessus, to recast the Fund as a poverty reduction institution is wrong-headed. It both conflicts with the World Bank's mandate and involves work that IMF staff members, who are more comfortable with central bankers, are not ideally suited to address. The IMF needs to focus on its role of crisis management and crisis prevention (including in the latter context making much better and more timely information available to markets and acting as the auditor for the auditors of banking systems).

Summits

Summits can be useful in two ways. First, they can help reduce security tensions – which can happen even in "photo op" summits, such as the Asia-Pacific Economic Cooperation (APEC) forum has tended to become. For example, there were significant benefits from the bilateral meeting between President Clinton and China's Jiang Zemin on the margins of the Auckland Leaders meeting in November 1999. Summits can also give direction to "line" institutions, especially when those institutions run into negotiating barriers.

Part II

The "Trade and ..." Agenda



Trade Liberalization: The Broader Context

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This paper was presented at a World Trade Issues Working Group seminar at the Department of Foreign Affairs and International Trade in September 1999. It builds on an earlier paper prepared for the APEC Economic Committee, The Impact of Liberalization: Communicating with APEC Communities *(APEC Study Centres Network and PECC Consortium for APEC, November 1998). The usual disclaimer applies: the views presented at the seminar and reported here are not to be attributed to the Department of Foreign Affairs and International Trade or to the Government of Canada.*

This paper provides an overview of trade liberalization and its interface with a number of contemporary issues and concerns. It consists of six sections: The Rationale for Trade and Liberalization; What Is Liberalization?; Trade and Policy Coherence; Trade and Adjustment; Trade and the Environment; and Liberalization, Governance and National Sovereignty. Each of these sections aims to bring out the linkages between the issues and the complexity of conceptualizing and assessing how liberalization impacts upon our lives.

The Rationale for Trade and Liberalization

The economic benefits of trade and trade liberalization are widely recognized. By improving the allocation of factors of production, trade is an important contributor to economic welfare.[1] Trade allows economies to move beyond domestic production possibilities and constraints, and in so doing to provide a higher standard of living than would otherwise be the case.

The benefits of trade can be illustrated with an intuitive example. Consider two economies: Korea and Indonesia. Korea has no domestic oil production and requires imported oil from Indonesia, or from other oil producers, to sustain its economic activities. Without this oil, the standard of living in Korea would fall. Conversely, Indonesia demands a range of consumer and capital goods not produced domestically, thus requiring imported goods from Korea, or from other goods producers. Without these goods, the standard of living in Indonesia would fall. Trade thus is beneficial to both of these countries.

Another way of understanding trade is to think of it as a technology for the production of goods.[2] Let us say there are two technologies for the production of cars in Canada. The first technology involves the physical production of cars in factories in the province of Ontario. The second technology involves growing wheat in the province of Saskatchewan and subsequently exporting this wheat to Japan in exchange for cars produced in Japanese factories. While the two technologies differ in respect to inputs used, the final result is the same: Canada has the cars. Consequently, whether Canada should use the first or second technology should depend on which one enables Canada to get the most cars (or to get the same number of cars with the least resources). Trade is like the discovery of a new technology that makes workers more productive.

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[1] It should be noted that the logic for international trade and for domestic trade are the same (i.e. division of labour and specialization). This logic may also be applied to individuals and trade among individuals. Without trade, each individual would have to be self-sufficient, and consequently would have an extremely low living standard and short life span.

[2] This example is taken from Marc T. Law and Fazil Mihlar, "Debunking the Myths: A Review of the Canada-U.S. Free Trade Agreement and the North American Free Trade Agreement," *Public Policy Sources*, no. 11 (The Fraser Institute, 1998). This approach to understanding trade is taken from James Ingram, *International Economic Problems* (New York: John Wiley, 1966).

The reduction or elimination of barriers to trade amongst countries encourages firms to produce and trade goods and services in which they have a comparative advantage. Economies will concentrate on goods and services that they produce efficiently, and trade these goods and services for what they produce less efficiently.[3]

Trade liberalization allows for the greater exploitation of economies of scale. By providing domestic producers increased market access opportunities, the freer market conditions enable firms to undertake specialized production runs that reduce the unit costs of production. For countries with small domestic markets, economies of scale may be extremely important. Economies of scale and specialization in specific product lines also explain why two or more countries may each produce and import and export a particular good, such as shoes. Each producer can have a specific market niche. This specialization in production, and the resulting increase in intra-industry trade (both imports and exports), however, implies change for the domestic industry.

Trade liberalization also increases competition in both the foreign and domestic markets. This implies that firms will need to respond faster to changing market conditions. Greater competition is likely to provide an incentive for firms to improve their economic performance through cost-saving innovations and to enhance the quality of their products. More competition also leads to lower prices for consumers. The core message of a recent OECD study is that, on balance, trade and investment liberalization in the long term is beneficial to society. The study gives a balanced assessment of the strengths and weaknesses of trade, including drawing attention to the fallacy of the argument that "exports are good and imports are bad." Trade liberalization influences both imports and exports. Access to low-cost imports, for example, plays an important role in enhancing consumers' well-being, as well as allowing domestic firms to have access to competitively priced inputs.[4]

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[3] The gains from trade depend on the pattern of comparative, not absolute, advantage. Even if Country A can produce everything more efficiently than its trading partner (absolute advantage), it will still have an incentive to trade if two conditions are satisfied: (a) it can produce certain things more efficiently than others; and (b) its own relative efficiency in producing some things versus others is different than the relative efficiency of Country B in producing these same product sets. This leaves room for Country B to produce those products that it can produce relatively more efficiently. Thus both countries have a comparative advantage in producing some goods and hence gain from mutual trade.

Finally, trade liberalization undertaken in a bilateral or multilateral context and which establishes clear trading rules will reduce uncertainty. Without such rules, a country may face unilateral, often damaging, actions from its trade partners. The reduction of uncertainty, while providing more stable access, will also allow firms to make more informed business decisions.

In short, an economy under autarky (i.e. one with no or limited international trade) that must domestically produce all that it consumes, forfeits the economic gains (and social benefits) that are realized through international trade. Trade, and the liberalization to make trade possible, is a positive proposition.

In an article addressing some myths and misconceptions of trade, Paul Krugman highlighted and summarized six points to consider in understanding trade:[5]

- International trade is an economic activity like any other and can be thought of as a production process that transforms exports into imports.

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[4] OECD, *Open Markets Matter: The Benefits of Trade and Investment Liberalization* (Paris: OECD, 1998).

[5] Paul R. Krugman, "What Do Undergrads Need to Know About Trade?" *American Economic Review*, 83 (May 1993).

- Imports, not exports, are the purpose of trade. A country benefits from trade because of the ability to import the products it wants. Exports are not an objective in and of themselves: the need to export is a burden that must be borne in order to pay for imports.
- High productivity is beneficial, not because it helps a country compete with other countries, but because it lets a country produce, and therefore consume, more. This is true in a closed economy, and it is no more or less true in an open economy.
- Too much emphasis is put on "high value" sectors. Trade allows all countries to benefit, not only those specializing in the "high value" sectors.
- Employment is a broad macroeconomic issue, with policies, such as tariffs, having little net effect. Trade policy should not be debated in terms of "phony numbers about jobs created or lost."
- Government support of a specific industry may help that industry compete against foreigners, but it also takes resources away from other domestic industries. International trade does not change the fact that government cannot favour one domestic industry except at the expense of others.

What Is Liberalization?

To understand trade liberalization, an understanding of the characteristics and institutional context of trade is required. The focus here will be on the multilateral trading system. The most visible trade barrier is the tariff, but trade liberalization is much more than negotiations on tariff rates. Within a multilateral context, first with the General Agreement on Tariffs and Trade (GATT) and then with the World Trade Organization (WTO), tariffs have fallen considerably over the past 50 years.[6] But other measures aside from tariffs, such as subsidies and government procurement practices, also affect trade. These have long been recognized as often having trade-distorting effects and requiring multilateral discipline.

The Uruguay Round of GATT negotiations, which resulted in the establishment of the WTO, expanded the multilateral trade rule framework to include such issues as trade-related investment measures (TRIMs), trade-related intellectual property rights protection (TRIPS), and trade in services. Services, which cover a wide range of economic activities such as banking, transportation and telecommunications, are an important component of the economy and of trade. While the details of the WTO's General Agreement on Trade in Services (GATS) are complex, the Agreement substantially broadened the economic activities subject to multilateral rules.

Dispute settlement is another important aspect of trade liberalization. Without an effective dispute settlement mechanism, trade liberalization measures become less secure and predictable for participants in the trading system. Yet the dispute settlement mechanism, while significantly different in nature from a tariff, also influences a firm's production decisions and how it approaches international trade. In considering the benefits of trade liberalization, capturing the benefits of dispute settlement and rules for such practices as anti-dumping measures is extremely difficult. The literature generally recognizes that a predictable and transparent global marketplace with an effective dispute settlement mechanism is beneficial to importers, exporters and consumers.

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[6] The General Agreement on Tariffs and Trade opened for signature on October 30, 1947. The GATT, containing tariff concessions and a set of rules preventing certain trade restrictions, was signed by 23 countries. On January 1, 1948, the Agreement was implemented. There were eight rounds of negotiations in the GATT. The seventh round, which began in 1973, is referred to as the Tokyo Round, and the eighth round, which lasted form 1986 to 1994, is called the Uruguay Round. J.H. Jackson, *The World Trading System* (Cambridge, Mass.: MIT Press, 1991) provides an insightful overview of the rights and obligations set out in the GATT. The World Trade Organization, which subsumed the GATT, was established by the Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations. It was implemented on January 1, 1995. The WTO currently has over 130 members. For a history of the Uruguay Round negotiations leading up to the establishment of the WTO, see John Croome, *Reshaping the World Trading System: A History of the Uruguay Round* (Geneva: World Trade Organization, 1995).

Multilateral discipline through rules and dispute settlement procedures is particularly important for smaller economies that do not have the economic power to resolve conflicts through bilateral means. This is a useful perspective, as some consider the multilateral trading system to be in the interest of the largest economies only. On the contrary, while the system is of interest to all economies, the smaller economies stand to lose the most from its deterioration.

Trade liberalization is also intricately tied to the "new" trade agenda dealing with a range of trade-related issues. There is no consensus as to what the scope of these issues is or should be.[7] As a practical matter, the WTO has not turned a blind eye to the "new" trade issues. While the WTO does not at present have a mandate to negotiate such issues, its members see a need to more fully understand the relationships between trade and other policy areas. Soon after its creation in 1995, the WTO formally established a Committee on Trade and the Environment; at its Singapore Ministerial Conference in 1996, the WTO agreed to create working groups on the relationship between trade and investment, and trade and competition policy linkages.[8]

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[7] U.S. Trade Representative (USTR) Charlene Barshefsky has highlighted competition law and restrictive business practices as barriers to trade. The USTR observed that with respect to Japan, "markets remain largely closed, opaque and driven more by informal cliques than by laws, rules and contracts." She also raised the issue of bribery and corruption and called for the WTO to "begin tackling head-on bribery and corruption." "Barshefsky Calls on WTO to Reduce Structural Barriers to Trade," *Inside U.S. Trade*, 16, no. 15 (April 17, 1998), 15.

[8] An earlier GATT group, the GATT Group on Environmental Measures and International Trade, had been active since 1991.

Trade and Policy Coherence

While liberalization of trade is an important component in improving living standards, it is only a component; a coherent set of policies is required to achieve a durable improvement in living standards. This is an important conclusion as it stresses that the overall balance of costs and benefits of liberalization depends upon choices made in other policy areas.

Trade and other international economic activities are linked with a complex mix of "domestic" economic, and even social, policies such as those addressing human resource development, economic infrastructure, environmental stewardship, adjustment to technology, and promotion of innovation.[9] Whether economies can seize, and benefit from, the opportunities afforded by trade liberalization in large part depends upon domestic policy decisions and how firms respond to these decisions. At the same time, the intersection of international trade with traditionally domestic policy areas raises increasingly sensitive questions of "policy coherence." This is particularly relevant and of broad public interest in respect to issues surrounding structural adjustment, such as labour market policies. Public interest is also high in regard to the linkages between trade liberalization and the environment.

Trade liberalization, by opening markets to increased competition and accentuating the ongoing structural adjustment process, makes the costs and benefits of domestic policy choices more transparent. Poor policy choices, however, with or without trade, have a cost. Turner emphasized this point with respect to Europe, by observing that Europe's unemployment problem is not due to a failure of competitiveness in the face of a global challenge, but due to a failure of economic flexibility in the face of developments most of which would have occurred even if trade and capital flows were no more global than in the 1960s.[10]

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[9] The nature of these links is not always clear or obvious. For example, bribery and corrupt business practices that distort competition and trade and investment are an issue. In an attempt to address corruption, in November 1997, OECD members adopted the Convention on Combatting Bribery of Foreign Public Officials in International Business Transactions. For an overview of the causes and consequences of corruption, see Kimberly Ann Elliot, ed., *Corruption and the Global Economy* (Washington, D.C.: Institute for International Economics, 1997).

Trade and Adjustment

Trade and trade liberalization by definition imply that the composition of production and employment changes in the countries involved. This, however, in no way implies that trade is the singular or most important factor contributing to pressure for labour force adjustment. Labour markets are in constant flux. At any given time, different sectors of the economy are growing or contracting at different rates. Nor should it be understood that changes in the labour force or pressure for change, from whatever source, are an adverse economic development. In a dynamic economy, social stability must be built around the process of "creative destruction."

The economic benefits stemming from trade liberalization require adjustment, including labour market adjustment. The OECD has summarized the empirical results of a number of studies conducted on the employment effects of trade liberalization.[11] It concluded that the net impact of trade liberalization on employment is in general small at the aggregate level of the overall economy. The labour adjustment required is also likely to be small with respect to changes occurring for other reasons, such as technological change or the emergence of new products. The OECD report concluded that "the number of additional workers who would have to change jobs as a result of trade liberalization would be likely to be only a fraction of the normal rate of labour turnover, particularly if the trade liberalization were spread over a number of years."[12] The central conclusion of the OECD work – that the role of liberalization in labour market performance is much smaller than many believe – has also been reached by others.[13]

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[10] Adair Turner, "Globalization: Threat or Opportunity," speech delivered at the European Business School, March 25, 1998.

[11] OECD, *Trade and Employment*, C(89)42 (1989).

Employment effects on specific sectors or firms could, of course, be more pronounced. The OECD also noted that social "problems may arise if the job displacements tend to concentrate on groups of the labour force who are disadvantaged anyway, e.g., unskilled labour."[14] From a political perspective, highly visible and concentrated sectoral job losses may not offset the more diffused job gains.

Trade liberalization implies that short-term structural adjustment is necessary for longer-term prosperity. This creates challenges for other policy areas, and raises the question of how governments can most effectively intervene to facilitate adjustment by firms and individuals to new conditions caused by change, including trade. It also raises the question of whether those experiencing pressure to adjust from foreign sources should be treated any differently from those facing pressure from domestic sources.

Analysts have noted that the type of trade and the type of structural adjustment pressures that occur can influence the public's perception of whether or not trade liberalization is beneficial.[15] Trade amongst OECD countries can be characterized as intra-industry (i.e. trade in similar products). Adjustment in this case involves shifting employment and other factors of production within a firm to new production lines, or shifts within an industry. There is no major de-industrialization of a sector, and the foreign competitors are not often regarded by the public as low-cost competitors with major differences in factor endowments.

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[12] OECD, *Trade and Employment*, C(89)42, Annex Summary Report (1989), 4.

[13] Lustig puts the concern and misperception of the role of trade into stark policy terms: "identifying ways to address the rising economic polarization and declining living standards for the less-skilled in the United States deserves greater attention on the part of policy makers. Otherwise, many lawmakers are likely to continue focusing on the wrong instrument – that is, trade protection – to combat it." Nora C. Lustig, "NAFTA: Setting the Record Straight," *The World Economy*, 20, no. 5 (August 1997), 606.

[14] OECD, *Trade and Employment*, C(89)42 (1989), 29.

Inter-industry trade, the trade of different products from different industries in different countries, is often associated with OECD member country trade with developing countries. This type of trade can require that adjustment be made by an entire industry. The entire workforce of an industry could face change due to new, low-cost producers. This type of industry adjustment, which is much more visible to the media, prompts demands from the industry and employees to remove the threat from foreign producers (i.e. demands for protection).

Nevertheless, protectionism is not a viable, long-term strategy for improving living standards.[16] Attempting to maintain a status quo industrial structure in the face of global change is a short-sighted strategy. High tariffs and levels of protection insulate domestic producers from competition; however, over time, as international competitors increase productivity, the gap between domestic and foreign producers grows, as does the gap in living standards between the economies. Also, the longer protection lasts, the more difficult it becomes politically to liberalize, as the adjustment shock to domestic producers will be greater. Moreover, even though adjustment is a "cost" in the short run, it is a "benefit" in the longer run. The final word goes to Lustig, who summarizes this view as follows:

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[15] Niels Thygesen, Yutaka Kosai, and Robert Z. Lawrence, *Globalization and Trilateral Labor Markets: Evidence and Implications, A Report to the Trilateral Commission*, 49 (December 1996).

[16] The OECD compiled a significant body of evidence on the cost of protection in a 1985 study entitled *Costs and Benefits of Protection*.

> It may be important to note that even if trade protection may bring small, short-term relief for unskilled workers, this will be at the expense of lower growth and living standards – including those of less-skilled workers – in the future. A more fruitful alternative would be to pursue policies designed to upgrade the education and skills of the working population.[17]

Trade and the Environment[18]

The public has expressed some concern that, through adverse effects on the environment (in terms of increasing pollution, accelerating resource depletion and contributing to the erosion of the environmental legacy), trade lowers the overall quality of life for both present and future generations.

Some of the trade-environment interactions are direct, such as the import and export of environmentally friendly or hazardous products. Others are indirect, such as the positive influence of trade on per capita incomes, which in turn stimulates demand for a cleaner environment, or the positive impact of trade on the level of economic activity, which in turn creates pollution.

When assessing the impact of trade on the environment, the stringency of environmental policy must also be considered.[19]

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[17] Nora C. Lustig, "NAFTA: Setting the Record Straight," *The World Economy*, 20, no. 5 (Aug. 1997), 610.

[18] The material in this section is developed substantially in Robert T. Stranks, "Trade and Environment: Post-Seattle Looking Forward," in the present volume.

[19] Analytical work by the WTO has concluded, "it is generally accepted that in order for these benefits to be realized, and for trade-induced growth to be sustainable, appropriate environmental policies determined at the national

Trade and investment are not necessarily adverse for the environment. When environmental policies are set appropriately, available evidence suggests that trade and investment usually will have a positive impact on the environment. When environmental policies are not set appropriately, trade and investment can aggravate environmental problems. A significant factor is the nature of the environmental policy itself.[20]

If prices for products are distorted, such as through subsidies, trade and trade liberalization may have an adverse environmental impact. This, however, does not imply that trade or trade liberalization should be avoided, nor that trade measures are the most appropriate response to subsidization of resource use.[21] Rather, appropriate domestic policies are required to avoid negative environmental impacts. In particular, subsidies to producers or consumers of energy and agricultural

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level need to be put in place." This arises as the most significant trade liberalization-environmental linkages pass indirectly through effects on levels and patterns of production and consumption. WTO Committee on Trade and Environment, *Environmental Benefits of Removing Trade Restrictions and Distortions*, Note by the Secretariat, WT/CTE/W/97 (November 1997).

[20] See John Beghin and Michel Potier, "Effects of Trade Liberalisation on the Environment in the Manufacturing Sector," *The World Economy*, 20, no. 4 (July 1997), 437. They conclude: "A major policy implication that emerges from the study is the need for coordination of environmental policies and trade liberalisation reforms. Although free trade can be beneficial to the environment in the case of formerly protected and inefficient (pollution-intensive) industries, it is difficult to determine a priori the environmental implication of the post-liberalisation division of labour in manufacturing activities. Economic theory alone cannot predict trade and production patterns in dirty activities in a world of many countries, commodities, and factors of production. Hence, the presence of environmental policies is instrumental in protecting the environment."

[21] For a discussion on some of the difficulties of using countervailing duties in response to "environmental subsidies," see Robert T. Stranks, *Pandora's Box?: Countervailing Duties and the Environment* (Ottawa: Department of Foreign Affairs and International Trade, October 1994).

products often contribute to trade distortions as well as having negative environmental implications.

Moreover, trade and investment in environmentally preferred products and services are important mechanisms through which liberalization can benefit the environment. The key to this relationship is technology, and what products embodying the latest technologies, and services providing technologies, imply for the environment. International diffusion of technology and the use of efficient (resource-saving) products can be facilitated by freer trade and liberal investment policies.[22] Technology and innovation issues also imply that the links between trade and the environment need to be considered in a long-run framework.

It is worth noting that trade and trade liberalization may be characterized as being one of four things in respect to the environment: (1) absolutely beneficial for the environment; (2) neutral in respect to the environment; (3) negative for the environment, but less negative than the same level of economic growth or developments that would occur over time in the absence of trade or trade liberalization; and (4) more environmentally negative than the same level of economic growth or developments that would occur over time in the absence of trade or trade liberalization. While (1) is clearly the preferred outcome, (1), (2) or (3) should be acceptable from an environmental as well as a trade perspective.

Liberalization, Governance and National Sovereignty

Trade liberalization, and in particular that aspect of it which involves rules setting out rights and obligations, has evoked fears on the part of a number of individuals and organizations that national policy autonomy, or even sovereignty, is being gradually undermined to the detriment of society. The OECD describes this concern as "the perception that increased global competition, underpinned by global trade and investment agreements, is eroding the capacity of governments to exercise national 'regulatory' sovereignty; that is, to independently determine national policy objectives and implement regulatory decisions on both economic and social issues."[23] Yet constraints on independent action, with no regard to international repercussions, should not be considered as an inevitably negative development.

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[22] John Beghin and Michel Potier, "Effects of Trade Liberalisation on the Environment in the Manufacturing Sector," *The World Economy*, 20, no. 4 (July 1997), 437.

Constraints on governments may be positive, as they add predictability to the conduct of international relations and allow for a worldwide trade regime to function.[24] In other words, the WTO is not a cost to be endured. Rather, it is a benefit to be actively supported.[25] For smaller economies that would otherwise be subjected to discriminatory trade policy actions from larger economies, this is particularly important. International commitments may also act as a counterweight to protectionist forces and short-term political opportunism.[26] To the extent that there is a dilution of unrestrained sovereignty, it can be offset through the use of influence by national governments in international organizations and the establishment of international rules.[27] Globalization, and the international governance that has accompanied it, should not be seen as the death of the nation-state nor as the reckless throwing open of vulnerable domestic economies to chaotic forces.

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[23] Organization for Economic Co-operation and Development, *Open Markets Matter: The Benefits of Trade and Investment Liberalization* (Paris: OECD, 1998), 76.

[24] This is not specific to trade liberalization. An important aspect of sustainable development and protection of the global commons is the recognition of the need for joint and co-operative measures that may restrain national action.

[25] It should also be recalled that the WTO is not a supranational organization, and that it only administers what its members have agreed to.

[26] This benefit is sometimes called the "Ulysses effect," where international rights and obligations help prevent governments from being tempted to favour interest groups at the expense of the economy as a whole. Kym Anderson, "50 Years: Looking Back, Looking Forward," paper presented at the Graduate Institute of International Studies and World Trade Organization, Geneva, April 30, 1998.

Trade liberalization and trade governance are manifested in internationally negotiated rights and obligations. Governance is about giving direction, but it is also about providing an analytical framework for issue formulation. In an international context, with the recognition that new policy tools and international co-operation will be required, former WTO Director-General Renato Ruggiero has characterized this governance challenge as the risks and benefits of "inventing the future."[28]

Does trade liberalization, or globalization more generally, require a dismantling of national social welfare mechanisms and a race toward minimal government? The answer to this is: "not likely." The fear that governments are being rendered unable to implement regulatory decisions on social issues is not supported by the evidence. Krugman and Lawrence have emphasized that governments retain substantial autonomy in regulating their economies, designing their social policies, and maintaining institutions that differ from those of their trading partners.[29]

With liberalization in the broad self-interest of economies, and not detrimental to the exercise of national sovereignty, why is it that countries maintain and at times strengthen restrictions?

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[27] This said, multilateral rules need to be clear and minimize uncertainty in the provisions of the agreement. This is fundamental to ensuring that a party to an agreement fully understands the rights and obligations of an agreement before signing on to it.

[28] Renato Ruggiero, "Charting the Trade Routes of the Future: Towards a Borderless Economy," speech given at the International Industrial Conference, San Francisco, September 29, 1997.

[29] Paul Krugman and Robert Lawrence, "Trade, Jobs, and Wages," *The World Economy*, 21, no. 4 (April 1994).

There appear to be two explanations. First, understanding trade and the links with the domestic economy is not an easy or straightforward task. Consequently, the public may be misinformed, and this is likely to translate into less political support for liberalization than would otherwise be the case. Second, there is a political economy explanation for protectionism.[30]

This literature draws attention to the fact that some firms and individuals gain, sometimes quite considerably, from protected markets. Protection influences the distribution of income, with the income gains being concentrated in the few who actively support political regimes that are willing to allow the protection to continue or even increase. The losses are spread over a large section of the public, and on a per capita basis are often not large enough to stimulate collective and co-ordinated action to act as a political counterweight to those seeking protection.

Based on the foregoing, the following six challenges are particularly relevant for the future of the World Trade Organization.

1. The first challenge is to preserve what has already been achieved during the 50-year period since the establishment of the GATT. In this regard, the WTO dispute settlement system has proved to be a powerful instrument for resolving complaints, either through bilateral consultations or through the panel process when consultations fail. Of particular note is that the developing countries are increasingly taking an active role, as witnessed by the fact that, in the last two years, about half of the WTO requests for consultations or panels have come from developing countries. However,

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[30] See Gene Grossman and Elhanan Helpman, "Protection for Sale," *American Economic Review*, 84, no. 4 (September 1994); Arye L. Hillman, *The Political Economy of Protection* (New York: Harwood Academic, 1989); and Bernard Hoekman and Michel M. Kostecki, *The Political Economy of the World Trading System: From GATT to WTO* (London and New York: Oxford University Press, 1995).

contrary to some complacent views, the stability of the multilateral trading system cannot be taken for granted; government resources are required on an ongoing basis to preserve the trading system – which is a separate issue from reforming it.

2. The second governance challenge is to bring new members fully into the multilateral system. When the GATT came into effect in 1948, it had 23 contracting parties, mostly industrialized countries. This was far from a global organization. During the next 50 years, a large numbers of countries have acceded to the GATT and in turn become members of the WTO. Currently, the WTO has more than 130 members, and about 30 countries, including China and Russia, are negotiating accession.
3. The third challenge is the "built-in" agenda embodied in the Agreement Establishing the World Trade Organization, which established starting dates for further negotiations, most importantly in respect of agriculture and services. Added to the substantive negotiating issues of this built-in agenda, and the challenge of establishing negotiating modalities to most effectively promote trade liberalization and to obtain early results, is the larger consideration of bringing into multilateral negotiations a balanced set of issues outside the scope of the built-in agenda.
4. The fourth challenge is to ensure that regionalism supports multilateralism. A large number of economies are party to regional economic frameworks, many of which involve preferential trade arrangements that are inherently discriminatory and can result in trade and investment diversion. Regional arrangements are not necessarily in conflict with a multilateral approach to trade liberalization. Such arrangements may be more feasible and offer an avenue for liberalization in areas that would prove extremely difficult in a multilateral context. Moreover, regional deals can also prepare the ground for subsequent liberalization in broader multilateral agreements.

5. Many public policy issues are increasingly recognized as having both domestic and foreign components. This reflects both increased interdependence of economies and pressure to use international trade rules to achieve objectives other than those that traditionally fall under the trade umbrella. These objectives can include linking topics such as labour standards, environment, human rights or even geopolitics (e.g. Helms-Burton). These issues raise new challenges for the multilateral trading system. The efficiency implications of using trade measures in particular needs to be considered. In this respect, governance of "new" trade issues will require a high degree of coherence, co-operation and co-ordination amongst international institutions.
6. Domestic capacity building and public awareness of governance opportunities and challenges is an essential foundation for unilateral and/or collective policy action. Underlying each of the governance challenges identified in this paper is the requirement of national governments to provide leadership and seek informed public support for an open rules-based trading system. Such support rests on the public having a realistic appreciation of the benefits of trade and investment liberalization, as well as the structural changes that such liberalization will encourage or necessitate. To develop such an appreciation, individual members of the public most also think about liberalization and its effects in both the short term and long term.

Conclusions

This paper has argued for a balanced overall view of trade liberalization. Liberalization is not the root cause of the world's economic ills, nor is it the panacea. Three key interrelated themes are worthy of highlighting. First and foremost, on balance, trade liberalization is, in the long term, beneficial to society. Liberalization promotes efficiency, encourages innovation, raises incomes and gives consumers a greater choice of goods. Liberalization is a means to an end, rather than an end in itself.

A second major theme is that while liberalization of trade is an important component in improving living standards, it does not stand alone: a coherent set of policies in other areas is required to achieve a durable improvement in living standards. This is important, as it stresses that the costs and benefits of liberalization depend upon choices made in other policy areas. This factor is particularly relevant with respect to issues surrounding structural adjustment, such as labour market policies and sustainable development.

Third, short-term structural adjustment is necessary for longer-term prosperity. This fact creates challenges for other policy areas. Most importantly, there is a need to facilitate adjustment, and for the gains from liberalization to be as widely shared as possible. This requires policies to help, in particular, those most affected by adjustment.

The concerns about trade liberalization inducing social disintegration are not justified. There is no evidence to suggest that liberalization is the main cause of income inequality. Rather, skill-biased technological change has increased demand for more-skilled workers and reduced demand for unskilled labour. Moreover, in the longer term, trade protection does not upgrade the skills of workers or contribute to a more flexible workforce, and this has its own negative social consequences. The appropriate policy response is to facilitate the adjustment of workers in increasingly knowledge-based economies, whatever the sources of change.

Addressing Trade-Related Development Needs: Options for the Donor Community

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Summary and Overview

The failure of the WTO Seattle Ministerial to launch a new broad-based round of trade negotiations focussed international attention on the role of trade liberalization in development, and the benefits and costs to developing countries of participation in the global trading system. Developing countries will be increasingly marginalized if they cannot attract foreign investment, do not have access to technology, and cannot take advantage of a rules-based multilateral trading system. At the same time, increased integration into the world economy means

new challenges in terms of institutional, infrastructural and human resource development.

These considerations have led Canada and other donors of development assistance to question the role that they should play in addressing trade-related needs of developing countries so that opportunities from trade and trade liberalization foster economic growth, leading to poverty reduction.

This paper looks at the linkages between trade liberalization, economic development and poverty reduction; discusses some of the constraints that affect the linkages between trade and economic growth on the one hand and economic growth and poverty reduction on the other; and draws some conclusions concerning the specific role that both donors of official development assistance and trade organizations can play in addressing these linkages.

The paper highlights three categories of assistance needed by developing countries in order for them to take advantage of trade-led economic growth. The first is specific to World Trade Organization (WTO) membership and refers to the technical and legal implementation capacity required by developing countries to address their WTO rights and obligations. The second category is private sector development, referring to the presence and ability of domestic private sectors to take advantage of opportunities from trade. The third category is that of an enabling environment in the form of appropriate governance, infrastructure and policies, which are essential to the efforts of domestic and international firms to translate opportunities from trade into economic activities.

These last two categories overlap with those needed for economic growth-led poverty reduction. Here, *private sector development* refers to economic practices that provide employment and income generation for the poor, while *enabling environment* focusses on governance, infrastructure and policies needed to support the ability of poor people to take advantage of economic opportunities and provide for their needs. Finally, targeted poverty interventions may be necessary to address the limitations of exclusive reliance on economic growth, and provide for the basic needs of those marginalized from economic activity and those unable to meet their needs based on current economic participation.

In considering how best to address these development needs, the paper recommends that the WTO, with substantially enhanced resources, concentrate on the delivery of membership-specific assistance, while private sector development, enabling environment and targeted poverty interventions fall to the donor community to address as part of overall poverty reduction programming. Co-ordination of the trade-related technical assistance activities of the WTO, its partners and development agencies could be modelled along the lines of the Integrated Framework for Trade-Related Technical Assistance to Least Developed Countries. Alternatively, co-ordination could be mandated to an independent organization.

Trade Liberalization, Economic Growth and Poverty Reduction

This paper asks the following question: What role should Canada and other donors of official development assistance play in addressing the trade-related needs of developing countries, so that opportunities from trade and trade liberalization can be used to foster economic growth that leads to poverty reduction? We answer this question by looking at the linkages between trade liberalization, economic development and poverty reduction, and at the specific role that donors and trade organizations can play in addressing these linkages.

The assumptions that guide this investigation are as follows:

1. Trade liberalization can foster economic growth.
2. Economic growth is essential for poverty reduction.
3. Economic growth, though essential, is insufficient for poverty reduction.

4. Poverty reduction is the mandate of CIDA and the majority of development organizations.

For poverty to diminish, trade must lead, in some form or another, to an increase in the resources available to the poor for the satisfaction of their basic needs. There are three mechanisms by which trade-led economic growth could lead to poverty reduction in developing countries: increased income and employment, improved provision of government services, and decreased cost of goods and services.

Increased Income and Employment

The main expected gain from trade is stronger economic growth, leading to employment and/or wage increases. This gain occurs through a variety of mechanisms, including an increase in private sector investment, productivity gains from technology transfer and skills training, and competition-induced domestic restructuring.

In concrete terms, economic growth means more jobs for workers who produce goods and services, or higher incomes (through wage increases), or both. These impacts are felt beyond the specific businesses engaged in trade, as they stimulate both upstream and downstream production linkages.

The competition and productivity gains associated with trade may have similar effects on employment and income generation in domestic (non-exporting) industries. These can arise, for example, as new imports stimulate technology transfer, provide more efficient and/or lower-cost intermediate inputs, provide lower-cost inputs into production, etc. Similarly, competition with foreign producers is expected to lead to more efficient domestic investment choices and business practices.[1]

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[1] Competition is, however, a two-way street, with some domestic firms forced out of the market, while others survive. The net effect on employment and income generation is unclear here.

Improved Provision of Government Services

Stronger economic growth should lead to increased government revenue through direct and indirect taxes, licensing fees, etc.[2] Some of this government revenue may be reinvested generally in the domestic economy and further increase employment opportunities. Other revenue, however, can be used to invest in new or existing targeted social spending and basic infrastructure of specific interest to key groups. Insofar as these investments lower the costs or increase the quality of the goods and services available to these groups, the overall cost of living will decline.

A further increase in public revenue and poverty spending may occur as a result of improvements in the effectiveness of governance brought about by trade liberalization. Indeed, the World Bank has identified trade openness as one of the characteristics leading to greater aid effectiveness.[3] As trade liberalization contributes to increasing government revenue, and to the ability of governments to better use this revenue, benefits to the poor can be anticipated.

Decreased Cost of Goods and Services

Liberalization can lead to the availability of new, lower-cost consumer imports, which may replace more expensive products previously consumed. Similarly, cost reductions in domestic production through lower-cost inputs and competition-induced productivity gains can reduce the cost of domestically produced and consumed goods and services. Taken together, these can reduce the overall cost of consumption for poor people who consume the affected products. Likewise, even though costs may not fall, improvements in the quality of goods and services also contribute to this process.

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[2] Here, too, we must be careful to factor in losses in government revenue through tariff reductions linked to liberalization (see, for example, L. Ebrill, J. Strotsky and R. Gropp, *Revenue Implications of Trade Liberalization,* International Monetary Fund, Provisional Agenda Item 4 of Commonwealth Secretariat Global Conference on the Development Agenda for Small States, February 2000).

[3] See *Assessing Aid – What Works, What Doesn't, and Why,* World Bank Policy Research Report, Oxford University Press, 1998.

In summary, we anticipate that trade will stimulate economic growth through a variety of positive, efficiency-promoting impacts upon domestic industries and the economy as a whole. This growth can result in increased employment and income-generating opportunities, more revenue for government spending on services and infrastructure, and a decrease in the price of goods and services. Insofar as the benefits are directed to the poor, there is little need to question the value of trade-related development assistance.

However, some researchers have found evidence that in some countries, at least in the short to medium term, poverty has not been reduced by trade liberalization and economic openness. For example, in their December 1999 paper, *The Simultaneous Evolution of Growth and Inequality,* World Bank researchers Mattias Lundberg and Lyn Squire find that in 38 countries, from 1965 to 1992, greater openness to trade is correlated negatively with both relative and absolute income growth among the poorest 40 percent of the population, but strongly and positively with income growth among remaining groups. The authors caution that "The adverse short-term consequences of openness to the welfare of the poor, and their vulnerability to terms-of-trade changes, compel us to pay greater attention to the disaggregated distributional consequences of policies in general and globalization in particular."

Constraints to Gains from Trade Liberalization and Poverty Reduction

These mixed impacts of trade liberalization on poverty reduction provide two challenges for trade-related development assistance. First, while trade liberalization and an enabling policy environment are important, there are circumstances where these are insufficient to foster stronger economic growth. Ensuring that trade liberalization actually does lead to stronger growth provides the first challenge for trade-related development assistance. Second, while economic growth in general is necessary to reduce poverty, there are circumstances where the poor may not be significant beneficiaries or may in fact be adversely affected. Making sure that trade-led economic growth does, in fact, lead to poverty reduction is the second challenge for trade-related development assistance.

Trade liberalization is ongoing in many developing countries. While some of these countries have prospered using trade as an engine of economic growth and poverty reduction, others have failed to secure the benefits described above. We explore below some of the reasons why trade liberalization has not led to poverty reduction, in order to identify constraints that may be addressed through trade-related development assistance.

A 1998 World Bank study lists the following conditions for using trade as an engine of economic growth:[4]

1. a sound macroeconomic environment;
2. an enterprise development plan to foster a dynamic private sector;

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[4] J. Michael Finger, Francis Ng and Isidro Soloagra, "Trade Policies in the Caribbean Countries: A Look at the Positive Agenda," World Bank paper prepared for Caribbean Group for Cooperation on Economic Development, Washington, D.C., June 1998, 10-11.

3. a corresponding human resource development program in both the public and private sector;
4. a trade facilitation program, including customs administration;
5. physical (transport, communication, electricity) and legal-institutional infrastructure; and
6. effective use of the WTO and other international instruments.

While it is clearly unnecessary to meet all of these conditions in order to gain from trade, many developing countries, especially those among the least developed, cannot meet any of them.[5] Similarly, many developing countries lack other characteristics related to productive capacity, including the availability of a sufficiently skilled labour force, enabling regulatory frameworks, modern financial sectors, etc. In the absence of these characteristics, trade openness alone may not lead to economic growth.

Even where these characteristics do exist at the national level, and trade does lead to economic growth (as it does in the vast majority of trading nations), the poor may not be beneficiaries of this process. In other words, there is nothing implicit in the structure of trade or trade liberalization that ensures that the positive impacts described above will be experienced by the poor, as opposed to the non-poor.[6]

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[5] In some cases developing countries *will not* develop these conditions, due to lack of political will and commitment to reforms. However, while these circumstances require different approaches to addressing the absence of these conditions, the fact remains that they continue to be a significant barrier to effective gains from trade.

[6] It is true that in many developing countries, the primary resource is an abundant supply of relatively low-cost labour. Insofar as trade in these countries results in economic growth in sectors or industries that absorb this labour pool, there will clearly be an impact on poverty, although even there the net effect may be reduced due to rural to urban migration, dislocation of non-competitive industries, poor labour and environmental standards, etc.

In a USAID working paper, the authors point out that the extent to which trade leads to poverty reduction depends to a large degree on where the poor live and the orientation of the government's strategy for the provision of social services and infrastructure.[7]

For example, since most industry-oriented trade-led economic growth takes place in urban centres, only poor people located in these centres are likely to benefit in a significant way. In Latin America, Eastern Europe and parts of Asia (excluding India and China) many, if not most, of the poor are located in urban areas, so their gains may be significant. However, in other parts of Asia, and in most of Africa, the majority of the poor live in rural areas. Indeed, on a global scale, it remains true that the majority of the poor are rural, not urban. While this group of people stands to gain considerably from liberalization in agriculture (which is proceeding at a much slower pace than liberalization in non-agricultural goods and services), insofar as the focus of trade-led investment remains primarily urban, many or most poor people may fail to benefit from the direct employment and income effects of trade-led economic growth.

Indirect benefits from government services and cost of consumption reductions may also be limited for the poor. Although some government programs explicitly target rural and marginal areas, in many cases government infrastructure and social spending, for obvious political reasons, is disproportionately oriented toward urban centres and non-poor neighbourhoods therein, once again missing the bulk of the poor population in many countries. Similarly, because the rural poor tend to consume more non-tradable domestic goods and services (products that are only domestically produced) relative to their urban counterparts, they are less likely to gain from falling consumer prices.[8]

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[7] *Trade, Economic Growth and Poverty Reduction,* U.S. Agency for International Development, Discussion Paper No. 1, 2000.

There are a variety of other issues raised by civil society groups concerned with the negative impacts of trade liberalization on vulnerable people and countries that, in combination with the warnings above, illustrate the costs and potential limits to the benefits of trade-led economic growth.[9] None of this is to deny that trade leads to benefits for large numbers of people; indeed, most studies have found positive correlations between trade openness and increases in per capita income growth.[10] Rather, we need to caution against taking the poverty-reducing outcome from trade as a given.

Trade-Related Development Needs

The evidence showing that trade liberalization can result in a more unequal distribution of income is an indication that the benefits of trade in many countries are disproportionately captured by the non-poor. However, less equitable income distribution may not be considered a problem in and of itself if overall poverty is declining (i.e. if incomes of poor people are growing, but at a slower pace than those of the non-poor). Nevertheless, as previously mentioned, some researchers have found that openness to international markets has reduced the income of the poor in some countries.[11]

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[8] The urban poor, whose consumption of tradable goods is higher than that of their rural counterparts (although still lower than that of the non-poor), may benefit to a larger extent.

[9] These include circumstances where trade-led growth is capital-intensive and fails to employ low-skilled workers; dislocation, through trade-induced competition, of existing workers and producers of goods and services who are unable to match their more productive international counterparts; and the exacerbation of an already unequal distribution of resources, due to which the poor cannot access the skills, land or finances that would enable them to take advantage of trade-related opportunities. There are also concerns about exploitative environmental and labour practices in the absence of enforced national standards, leading to short-run gains and long-run losses for individuals and society as a whole.

[10] See, for example, the March 2000 World Bank paper, *Growth* Is *Good for the Poor*, by David Dollar and Aart Kraay.

These observations lead us to the question of what the international community can do to ensure that (1) trade liberalization does indeed lead to economic growth; and (2) trade-led economic growth leads to poverty reduction. We highlight two categories of support that may be required.

Trade Liberalization-Led Economic Growth

The first category of support corresponds to the ability of countries to use WTO membership, and their private and public sectors, as mechanisms that enable trade and trade liberalization to contribute to economic growth.

Trade and WTO membership: Many developing countries lack the technical, legal and administrative capacity to exercise their WTO membership rights or to fulfil their WTO obligations. Assistance in this area would enable developing-country members to better use WTO disciplines to their advantage in securing gains from international trade. Specific needs include:

- improved understanding of WTO rights and obligations;

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[11] In addition to the report by World Bank researchers Lundberg and Squire, noted earlier, see Barbara Stallings and Wilson Peres, *Growth, Employment and Equity: The Impact of Economic Reforms in Latin America and the Caribbean,* UN-ECLAC, forthcoming from Brookings and ECLAC, Spring 2000.

- help in drafting and implementing legislation and regulations to comply with WTO obligations;[12] and
- technical expertise to participate in trade negotiations, WTO committee activities and trade policy reviews, as well as to use the trade dispute mechanism effectively.

Trade and private sector development: In many developing countries, the formal private sector is insufficiently developed to take advantage of the opportunities from improved market access negotiated in trade-liberalizing agreements. Furthermore, the generally much larger informal sector may be constrained from formal participation. Assistance in this area would include provision of technical and legal expertise to facilitate international market participation

Trade and enabling environment: The successful development of the private sector and its subsequent involvement in international trade depends to an important extent on a supportive public policy framework and a functional economic infrastructure. Assistance here would include support for:

- development of government capacity (including both parliamentary and bureaucratic capacity);
- essential physical economic infrastructure (roads, ports, communication systems, etc.);
- legal and financial institutional infrastructure; and
- implementation of social (e.g. labour standards), environmental and gender policies and programs that are also associated with faster and more sustainable growth.

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[12] Given the significant financial costs of implementing the WTO, additional financial resources may also be required. This is especially true if the poorest WTO members are to avoid facing a trade-off between poverty reduction programming and WTO obligation implementation. See J. Michael Finger and Philip Schuler, *Implementation of Uruguay Round Commitments: The Development Challenge* (Washington: World Bank, October 1999).

Economic Growth-Led Poverty Reduction

A second category of trade-related development needs corresponds to factors that determine the ability of countries to use the economic growth facilitated by trade and trade liberalization in order to reduce poverty and faclitate efforts of poor people to gain access to productive assets, employment and income-generation opportunities.

Poverty and private sector development: Attention here is directed toward integration of the informal economy (where more of the poor work) into the formal economy, where better opportunities exist. Incentives for the private sector to participate in global trade in ways that are more beneficial to the poor can contribute in this regard (e.g. adopting low-skill, labour-intensive production processes).[13]

Poverty and enabling environment: The emphasis here is on adaptation of public policies, services and infrastructure, including financial services oriented to micro credit, to address the challenges of access by the poor, and especially poor women, to economic opportunities. A poverty lens also needs to be applied to social, environmental and gender equity policies and programs.

Poverty and targeted interventions: For a variety of reasons, many poor people may not be able to participate in the market economy. There may also be new groups of poor created by the structural reforms associated with trade-led economic growth. As a result, interventions are needed to specifically target the needs of both those who are marginalized within economic systems and those who cannot, even within current economic systems, meet their basic needs. Through a focus on access to productive resources, better health, education and empowerment, this area of assistance may foster the conditions for their future market engagement.

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[13] There is some controversy in this last regard, in that over the long run, development history has shown that labour-intensive processes tend to be inefficient relative to capital-intensive techniques. This implies that as the relative cost of capital declines, in part due to the process of liberalization itself, and as competitive capital-intensive goods displace low-productivity substitutes, low-skill employment generation may become ever more difficult to promote (from private correspondence with Nizar Assanie).

An International Division of Labour for Trade-Related Assistance

As can be seen from the above discussion, there is a great deal of overlap between needs corresponding to trade-led economic growth and those corresponding to economic-growth-led poverty reduction. This observation is significant since it is precisely by focussing on the areas of overlap that donors can best leverage scarce development resources in support of both economic growth and poverty reduction. This paper makes two recommendations for the division of trade-related assistance that would leverage the relative expertise of bilateral donors and multilateral agencies.

Recommendation 1: donor assistance: We recommend that donors of development assistance target their trade-related resources toward those activities that are known to facilitate both trade-led economic growth and economic growth-led poverty reduction.

Recommendation 2: WTO membership: We recommend that the World Trade Organization, primarily through non-aid resources derived from assessed member contributions and private sector donations, direct the provision of the technical assistance required so that all developing countries (both members and those waiting to accede) can understand and meet their obligations, and can understand and exercise their rights of membership in the WTO.

We address each of these recommendations in turn.

Donor Assistance

Donors should focus on trade-related capacity development, which is known to have benefits for the poor.[14] We agree that trade liberalization can lead to economic growth and that economic growth is an essential contributor to, although not a guarantee of, poverty reduction. We have also identified a number of constraints that impede the success of some countries attempting to use trade liberalization as an engine of economic growth, and economic growth as a tool for poverty reduction. There is thus an obvious need for assistance that addresses these constraints.

The question then becomes who should address which constraints, with the answer depending on the mandate of the providers of such assistance. As stated previously, donors of official development assistance have a poverty reduction mandate. These donors have scarce financial resources to devote to this mandate. Therefore, donor assistance should be directed toward interventions that have the greatest impact on poverty reduction.

Although membership in the WTO addresses some constraints to gains from trade, we believe that assistance for private sector development and enabling environment, from both a trade and a poverty reduction perspective, will have a broader impact on key constraints to economic growth and poverty reduction. This latter set of needs is thus the optimal target for trade-related development assistance.[15]

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[14] We recognize here that not all activities by donors are subject to a poverty reduction mandate. For example, within CIDA, the Central and Eastern Europe Branch does not require poverty reduction.

WTO Membership

In the absence of donor assistance related to WTO membership, other organizations will need to address these needs. Those best suited to providing the specific legal and technical advice needed for implementation of trade agreements and participation within the WTO are the WTO itself, and member state public and private sector organizations with experience in the global trading system. These organizations should work together, under the direction of the WTO, to provide the membership-specific technical assistance required for full participation by developing countries in the rules-based multilateral trading system.

Although the WTO, as the organization that oversees the implementation of the rules of multilateral trade, is the obvious choice for a centre of expertise to address developing-country membership needs, it is also a small organization with limited personnel and even more limited financial resources. This being the case, its trade-related technical assistance capacities need to be expanded considerably, albeit within a very narrow focus. The responsibility for providing the resources for this expansion lies with WTO member states themselves, which have previously committed themselves to providing these resources, either through the WTO proper or through their own government programs.

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[15] By this recommendation, we are not suggesting that donors cease to address other poverty-related needs, nor that they restrict their enabling environment and private sector support to only trade-related activities.

There is little doubt that, in spite of their promises, members of the international community have not kept up with the demand for financing and technical assistance needed to address developing-country needs with respect to WTO membership. It is now their responsibility to do so, through supporting the WTO in addressing membership-related needs, and supporting donor agencies in broad development capacity building. In the event that public resources remain insufficient, the WTO should turn to private sector companies (strictly through a trust fund mechanism) that stand to gain the most from full participation in trade by developing countries, so that these companies can fund the technical assistance that their domestic governments are unable or unwilling to support.[16]

Co-ordination and Coherence

These recommendations are intended to ensure that each type of organization delivers the trade-related assistance that best conforms to its organizational mandate and expertise. However, as previously mentioned, we acknowledge that WTO membership-specific needs and enabling environment or private sector development needs are related. Indeed, we have already accepted that both are linked to economic growth, which is necessary for poverty reduction. From a development perspective, efforts aimed at addressing WTO membership needs should be consistent with an understanding of the linkages between economic growth and poverty reduction.[17] Likewise, efforts to promote poverty reduction should be consistent with an understanding of membership-related needs. This being the case, both donors of development assistance and providers of WTO membership-specific assistance will greatly benefit from co-ordination and co-operation, to ensure that activities are as coherent and complementary as possible.

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[16] The idea of private sector funding was first suggested by WTO Deputy Director-General Andrew Stoler. While we admit that it would be extremely difficult to set up a system acceptable to both developing countries and supporting corporations, and that there could be considerable free-rider problems, the idea deserves further exploration as long as public funds remain insufficient.

This requires a further level of international co-ordination. The Integrated Framework for Trade-Related Technical Assistance to Least Developed Countries may provide a model that can be adapted to ensure that all actors in the area of trade and development work together. Alternatively, an independent organization could be granted the mandate of overseeing the trade-related technical assistance activities of the WTO, its partners and development agencies.

Further Needs and International Opportunities

As stated at the outset, the eyes and ears of the international community are focussed on trade and development. This issue was prominent at the April 2000 World Bank and International Monetary Fund spring meetings, and will remain high on the international agenda. The more general issues of globalization and its impacts are likely to remain a rallying cry for the civil society groups that massed in Seattle and Washington, D.C., and that intend to continue voicing their concerns.

While the degree of attention to these matters can make discussions difficult, it also provides an opportunity to suggest new ways of confronting challenges and to secure support for efforts that both address the needs of developing countries and reinforce the strength of the multilateral trading system. Some of the questions that have been raised in this paper require further exploration, as do the recommendations.

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[17] This is likely to be true as well from the perspective of maintaining support for the WTO and global trade. In the absence of clear benefits to poorer countries, the potential for a backlash against multilateral trade is significant.

The trade and development community needs to further address:

1. the causal relationships (both positive and negative) between trade liberalization and economic growth, on the one hand, and trade-led economic growth and poverty reduction on the other;
2. the best ways of addressing constraints that interfere with the positive causal relationships, and solutions to the problems arising from the negative causal relationships;
3. the optimal sequencing of reform implementation so as to minimize negative impacts on income distribution and poverty;
4. the actual value of WTO membership (as opposed to trade liberalization) for the smallest, economically weakest members, given the absence of financial and technical assistance in implementation of WTO obligations;
5. the value added of the individual actors in the trade and development communities in responding to identified needs; and
6. the optimal means for ensuring co-ordination and complementarity in the efforts of these trade and development organizations (internationally, nationally and within the organizations themselves) in order to achieve the ultimate objective of promoting prosperity for all.

Trade Liberalization: Culture, Identity and Social Cohesion

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Introduction

> *The challenge in this era of globalization – for countries and for individuals – is to find a healthy balance between preserving a sense of identity, home and community and doing what it takes to survive within the globalization system.* (Thomas L. Friedman, *The Lexis and the Olive Tree*, 1999: 35)

According to a recent public opinion survey, *The State of Affairs in the Nation Today* (The Goldfarb Report 1999), 73 percent of Canadians now support the North American Free Trade Agreement (NAFTA) and 65 percent support Canada's participation in trade agreements in general. Canadians think that the impact of trade agreements is beneficial to our economy, particularly because they believe it provides them with greater product selection. Moreover, a majority of citizens think that increased trade (both exports and imports) with other countries will result in more jobs for Canadians. However, the survey also notes that many Canadians do not believe that they have a firm grasp of this issue. Trend data on the impact of the World Trade Organization (WTO) and the General Agreement on Tariffs and Trade (GATT) show that two out of five Canadians say that they do not know what the impact of the WTO or GATT will be.

Despite the growing support for freer trade, the recent, sometimes violent, public protests at meetings in Seattle and Washington demonstrate that there is growing concern that the benefits of freer trade for society as a whole may be outweighed by the costs. In addition to economic costs and benefits, trade liberalization has an impact on many other aspects of our society: the environment, population movements, health, dissemination of knowledge and expertise, national identity, political and cultural sovereignty and social cohesion.

Some critics see international trade agreements as impinging on national sovereignty and posing a threat to basic social policies and programs, social solidarity and the distinctness of national identities. There has also been a strong public reaction against the power and influence of "faceless" transnational corporations and a perception that international regulatory institutions, such as the WTO, are undemocratic. The growing realization that decisions taken in the context of international trade have wider implications for such things as culture, environmental and labour standards and human rights has pitted the interests of business against the interests of social activists and other groups, causing social conflict and placing the WTO and other international institutions in the uncomfortable position of having to arbitrate on issues outside their envisioned mandates and areas of expertise.

This paper is not intended as a treatise or as a presentation of original research, but rather as a review of a representative selection of the most recent literature reflecting a wide range of domestic and international thinking on how trade liberalization affects culture, identity and social cohesion. It will examine the major issues relating to three sets of questions:

1) What impact is trade liberalization having on Canadian culture and specifically on Canadian cultural industries?
2) How is trade liberalization affecting the legitimacy of the nation-state as a repository of distinctive, common cultural values? What impact is trade liberalization having on national identities? Is homogeneity of the world's culture one possible eventual result?
3) What are some of the short- and long-term impacts of trade liberalization on social cohesion? What role does the nation-state play in mitigating these impacts?

This review of the literature will be followed by a discussion of how trade/culture issues are being addressed by international organizations and a summary of new strategies that have been proposed to deal with these issues in Canada.

Free Trade and the Cultural Industries

American cultural influences can now be found in even the remotest corners of the world. Geographically, Canada is the least remote corner of the world in relation to the United States. Given this geographical proximity, a common language shared by the majority of their citizens, common historical roots and many common influences on legal and political traditions and economic development, it is not surprising that the influence of American popular culture on Canadian culture, particularly English-Canadian culture, is overwhelming. Maintaining a flourishing Canadian culture has been and continues to be an important challenge for individual creators, the cultural industries and policy makers. As the 1987 federal policy paper, *Vital Links: Canadian Cultural Industries*, asserts:

> The bond that holds Canadians together is our distinct culture – not just in the sense of the arts, but in the larger meaning of our pastimes, habits, images, institutions, perspectives on the world, collective memory and our bilingualism and multiculturalism. Our culture is to a large extent the expression of who we are. (1987: 77)

Vital Links concludes that Canadian culture is "active and assertive"; however, it also suggests that the instruments of communication of this culture, the cultural industries, face difficult competitive odds. How, then, in this period of global economic integration, can we ensure the development of healthy and competitive cultural industries?

> There is a vital need in Canada to ensure that the burgeoning cultural development in the creative sense be marked by the development of healthy instruments of communication. Without them, creativity could still take place, but fewer Canadians would have access to these creations. The most evident need is to help join the creator in Canada to his or her audience. The cultural industries are the conduit. (77)

Recognition of this vital need to develop and maintain healthy Canadian cultural industries was one reason for negotiating an exemption for culture in the Canada-United States Free Trade Agreement (FTA). Yet, since the coming into force of the FTA in 1989, the effectiveness of the cultural exemption has been the focus of a great deal of discussion and criticism. Is it achieving its intended purpose, enabling Canadian "cultural" industries to flourish in a market dominated by American "entertainment" industries? If it is not, is there a better strategy to address this challenge?

In an article published only two years after the signing of the FTA, "Trade Liberalization and the Political Economy of Culture: An International Perspective," Graham Carr addresses three issues that he feels are fundamental to a reformulation of the Canadian position on free trade and culture: first, by exploring the nature and extent of American government involvement in culture in relation to Canada's strategy of "exemptionalism" pursued in the FTA; second, by examining the relationship between the U.S. position on culture in the FTA negotiations and the larger context of American foreign and commercial relations; and, finally, by considering how culture is treated in various international trade agreements involving countries of disparate size, wealth and power. (1991: 3-4)

Carr notes that some misgivings about the FTA stem from discrepancies between the official Canadian and American interpretations of the agreement. While Canada stresses that the FTA protects indigenous culture by exemption, the United States maintains that this measure is protectionist and is offset by a second provision that justifies retaliatory measures. There are also several unresolved issues not addressed in the FTA, including the definition of subsidies, the Canadian review of foreign takeovers and protection of intellectual property, as well as the allowable parameters for the discussion of these issues. (1-2) Despite these ambiguities, Carr feels that one thing is clear – Canada is again being put on the defensive in the cultural sphere. Yet instead of developing fresh ideas to deflect this pressure, Canadian commentators seem inclined to restate their old positions in order to "educate" our trading partners and convince them that the onus for accommodation is on them. (2-3)

Carr believes that by becoming better educated about American cultural policies and their importance in the context of larger U.S. commercial and diplomatic interests, and by becoming more attuned to the cultural dimensions of other international trade accords, Canadians will be better able to answer some of the fundamental questions raised by the FTA about the nature of culture and its relationship to trade liberalization. (5) The goal of his paper is to propose an analytical framework out of which might emerge an adequate response to American challenges and a better ability to advance Canada's cultural interests in the future. (5)

Turning to the FTA itself, Carr notes that although cultural industries are exempted under Article 2005(1), cultural issues intrude in several other places: elimination of duties on certain cultural products (Article 401); facilitation of cross-border telecommunications and information flow (Annex 1404 C); entry restrictions for persons engaged in certain cultural activities (Annexes 1408 and 1502(1)); restriction of foreign ownership in communications and cultural industries (Articles 1607(1) and 1607(4)); strengthening intellectual property protection (Article 2004); adjusting copyright legislation for cable transmission (Article 2006); repeal of certain sections of income tax legislation pertaining to advertising deductions in Canadian periodicals (Article 2007); dispute management mechanisms that may affect certain areas of culture (Article 2011); and which cultural industries are covered by the agreement and which are not (Article 2012). (7)

Carr concludes that "As far as Article 2005 goes, therefore, FTA is the diplomatic equivalent of squaring the circle: culture may be exempted from the agreement, but 'it most assuredly has not been left out.'" (7-8) Furthermore, he notes that critics of the agreement feel that Article 2005(1) is rendered irrelevant by Article 2005(2), which allows retaliatory measures of "equivalent commercial effect," meaning that not only could it negatively affect non-cultural sectors of the economy for "affirmative action" taken to protect culture, it might also discourage the government from supporting culture altogether. (8) He also believes that these fears are compounded by Article 2011, which outlines procedures for dealing with measures perceived by either party to be discriminatory, measures that do not apply to section 2005 but do apply to other sections of the FTA involving culture. (8)

As Carr illustrates, contrary to popular belief, the United States has a long history of government intervention in providing support for culture (funding, regulation and protective measures), and "From the vantage point of free trade, it is equally relevant to acknowledge the broad policy similarities which exist between the two countries by recognizing that 'a fully articulated system' of support for culture exists in the United States, and that government is instrumental in its success." (18) He suggests that "Canada would be better off if it reminded the United States of its own historical tradition of government aid to culture, and emphasized the genuine similarities which characterize current policies on both sides of the border." (18)

Carr also suggests that Canadians have failed to recognize the importance the United States attaches to culture as part of its larger foreign policy agenda because the American approach to culture in international affairs is different from our own, the definition of culture being linked to the free flow of information, technology transfer, exchange of services, and protection of intellectual property and connected to the doctrine of free trade. (19) He feels that "By harping on the fact that the two countries are each other's principal trading partners and extolling the special relationship they profess to enjoy, Canadians overlook the importance of global considerations in the development and deployment of American policies regarding Canada." (19) Carr feels that the Canadian preoccupation with cultural industries and markets within the context of the FTA has obscured the possibility of seeing that American interest in the cultural provisions of the FTA transcends the relationship with Canada and is of larger importance in setting a precedent for bilateral and multilateral negotiations with other countries. (19-20)

> By establishing the principle that culture is a commodity, by associating culture exclusively with industry, by formalizing a commitment to the transnational trade in knowledge, by liberalizing trade and information in cultural services, and by initiating the process for a comprehensive undertaking on intellectual property, the United States has furthered its global cultural interests through both direct and indirect means. In the process it has also set a precedent for follow-up negotiations on culture with Canada, and laid a basis for future bilateral and multilateral agreements with other countries. (29)

In order to adequately prepare for follow-up negotiations on culture-related issues, Carr feels that Canadians must transcend their obsession with national identity and focus on the political economy of culture in the broader context of American international affairs, realizing that "the fundamental issues raised by FTA concern the nature of culture and its relationship to information, technology, services, commodities, and property." (29)

Carr believes that comparison of the FTA with other trade treaties, such as the Convention Establishing the European Free Trade Association (EFTA), the Ireland-United Kingdom Agreement Establishing a Free Trade Area, and the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA), is required, not only because it reveals that the issues at stake are not unique, as might appear at first glance, but because it establishes both technical and political reference points that may prove useful in the implementation of the FTA. (30) While culture received scant treatment when these agreements were drafted, they nevertheless included measures directly related to culture such as the right to protect intellectual property and copyrights, public morals and national treasures of artistic, historical and national value, issues that have recently taken on heightened economic and political importance. (34)

Despite the vagueness and contradictions typical of many aspects of cultural policy contained within them, Carr feels that Canada can draw useful conclusions about the difficulties of assimilating culture into free trade agreements. (37)

> Above all, case histories of these agreements demonstrate that trade agreements are meant to be altered. If experience is any guide, there is little reason to expect that Article 2005(1) will be a permanent solution to Canadian cultural anxieties. Similarly, the failure of these agreements to reach anything like a comprehensive policy on culture is indicative of the extraordinarily complex nature of the challenge. (37)

Carr concludes that the debate on culture "increasingly revolves around its meaning in relation to other forms of knowledge, and the altered value of cultural production to the changing structure of the global economy." (38) Underlying these issues are ideological disputes about the benefits of state policy versus private enterprise, individual rights versus the public interest. (38) In order to effectively meet the challenges posed by free trade, Carr is convinced that "Canadians must break away from the nationalist paradigm which has traditionally determined their thinking on culture and examine the political economy of culture in an international context." (38) In his view, the problem with focussing on preserving sovereignty alone, although it is an important issue, is that it masks the complexity of cultural questions raised by the doctrine of free trade. (38)

In 1994, the *Canadian Journal of Communication* devoted a special issue to the subject of cultural development in an open economy (volume 19, 3/4). This collection of papers was written in response to an initiative by the Social Sciences and Humanities Research Council (SSHRC) in co-operation with the federal Department of Communications (now Canadian Heritage). The papers focus mainly, though not exclusively, on the cultural industries rather than on issues related to culture in its broader sense because the authors felt that in an era of mass communications and current global economic trends cultural industries face particularly long odds. I have chosen to summarize four papers from this collection that I feel deal with cultural issues in the broader sense.

In the first paper, "Of Culture, the Economy, Cultural Production, and Cultural Producers: An Overview," Rowland Lorimer and Nancy Duxbury adopt a sense of culture that "emphasizes the distinct set of values of Canadians and their embodiment in social, cultural, and political institutions, statutes, and practices, as well as our patterns of behaviour both as audience members and producers." (1994: 260) Culture is seen as "everything that can be shared" (261), not derivative of other forces but rather a primary element in the creation of human communities. In the context of an open economy, this means that culture "fully encompasses the economy, including the perspectives on life and work the economy encourages, the patterns of life it demands, and the selectivity of its visions." (261)

Lorimer and Duxbury note strong biases operating on both sides of the discussion of cultural issues arising from Canada's open economy. A strong economic bias commonly derives from the notion that since economics is the study of scarcity, it is, therefore, relevant at all levels and to all types of decision making in society. A cultural bias views economics as useful for understanding certain categories of behaviours but questions giving economic ideas priority over all others or extending economic ideas as foundational elements into other realms of society. (274) They also feel that, in order to better understand the different approaches to cultural industries adopted by various countries, it is important to examine the underlying philosophies guiding cultural development policies and programs. They define four basic models that have informed cultural policy in Canada and around the world:

a) the *community development/animation model* – based on belief in the value of information and self-knowledge and oriented to the idea of the community representing itself through various mediums that raise self-awareness;
b) the *cultural development model* – aimed at making accessible to the greatest number of citizens the outstanding works of humanity, ensuring the largest possible audience for national cultural heritage and favouring the creation of such works;
c) the *public service model* – aimed, more conservatively than in the cultural development model, at the preservation and promotion of national heritage (values and artifacts), especially through publicly funded institutions; and
d) the *market model* – both the current *global market model,* directed toward a free global market ever less hampered by governments, and the *cultural market model,* aimed at promoting merit goods, countering the effects of market failure or protecting infant industries by intervening in the market to apply correctives in the name of cultural development. (265-269)

In their view, the cultural development model is perhaps best exemplified by the approach taken by France; the public service model, by the United Kingdom; and the global market model, by the United States. (265-269) They see Canadian policies and programs as based on both the Canadian experience and the experiences of other countries – the United Kingdom, the United States, France, Australia and the Scandinavian countries – and, as such, as being both derivative and original: "derivative in the sense that they take into account the actions and analysis of other countries, original in the sense that they respond to the realities of the Canadian scene." (269) Generally speaking, with the exception of broadcasting policy, Lorimer and Duxbury feel that the cultural market model best describes the approach underlying current Canadian policy and programs. They note that Canada has also drawn on the community development model, although they feel that this philosophy has faded somewhat from the mainstream research and writing about culture. (265-269)

The difference in approach taken by Canada and the United States on the treatment of cultural industries in trade agreements can, in their view, be traced to the founding principles of each nation. "On the United States side the foundations of this approach to cultural industries reach to the Constitution and the Supreme Court. (Head and Sterling, 1990, p. 464) On the Canadian side the roots are more nebulous but equally basic. They are to be found in nation-building, the public interest and cultural sovereignty." (278)

> Canada's position starts with culture, acknowledges the industrial nature of cultural production in our modern information economy, and ends with cultural goals which may be achieved in part by industrial means. The U.S. position starts with markets, speaks in the language of free trade, property rights in copyright, free speech, free flows of information, consumer rights, and entertainment products, and ends with markets. Their practice is dramatically different. Private foundations support cultural activity, employment restrictions are endemic, the courts are often used to harass competitors, and certain laws may be invoked unilaterally when politicians can be persuaded to act. (277-278)

The authors also note that, under the current trade regime, Canada's bargaining power is not substantial. The coercion that can be mounted against us to live within the American interpretation of the GATT makes it appear as if our bilateral agreements (FTA and NAFTA) are the main source of our difficulties (275). "Given the size, power, social and political philosophy, and inclination of the United States to insist that other countries conform to its viewpoint rather than vice versa, the opening of our economy primarily to the United States, and then to the rest of the world means a lessening of our government involvement in organizing the economy, and in any activity that can be argued to be economic in consequence, particularly culture." (275-276)

In terms of socio-economic and socio-cultural implications, the authors believe, "An open economy changes the universe of choices for producers, consumers, and governments to the degree that they orient to it. In some cases it forces such changes." (276) They predict that this will result in an enhanced consumer loyalty at the local as opposed to the national level and an increased orientation to the international with the greatest diminution of regional and national loyalty in the economic sphere followed by a diminution in the social arena. (277) They suggest that product planning, design, marketing and distribution require transnational thinking, just as consumers and workers will have to reconsider their choices in a transnational context. (276)

In overview, Lorimer and Duxbury feel that the literature on Canadian cultural development philosophy, policy and programs is mostly commentary, outlining the evolving positions of the main players but containing little formal research. (272) They note that information on Canada's cultural industries is neither extensive nor thorough – nor is it being continuously generated; and that, on the whole, we are not very far along the path in gaining this information. (285) They believe that research which can inform the understandings, philosophies, policies and programs for cultural development in an open economy begins with a full understanding of culture and proceeds through:

- a conception of the relationship between culture and cultural development;

- the nature of spontaneous and deliberate cultural development;
- the historical and contemporary nature of cultural development and its philosophies, policies and programs;
- an understanding of Canadian cultural particulars and their changing nature;
- the nature of Canada's opening economy and the cultural orientation of our free trade partners as well as that of major trading blocs;
- the nature of the interaction between culture and the economy;
- the potential need for stimulation of integrative activities as well as activities that affirm the distinctive groups within Canadian society;
- the full nature of the structure and infrastructure of cultural development and cultural industries; and
- the educational preparation and sustaining mechanisms for cultural workers. (285)

In their paper, "Cultural Development and the Open Economy: A Democratic Issue and a Challenge to Public Policy," Marc Raboy, Ivan Bernier, Florian Sauvageau and Dave Atkinson begin by observing that economic globalization poses an unprecedented threat to public policy in the area of culture by upsetting the fragile balance between economics and culture. They feel that the role of the state is to redress this balance through policies that promote cultural development, essential not only to national culture and identity, but also to democratic public life. (1994: 291) They acknowledge that their view is clearly a "positioned one" and that, for some, cultural development refers only to the development of cultural industries – their concern is for the social aspects of culture. (293) "The democratic stake in cultural development is to re-establish the citizen's right to contribute to public life and, in this respect, to promote access to and participation in the cultural sphere" which, the authors maintain, "is increasingly centred in the mass media." (291)

Noting the efforts of several European countries, led by France, to exclude culture from the 1993 GATT negotiations, the authors point to the increasing focus on cultural matters as a point of friction in the developing global economy. (292) They suggest that with the liberalization of international trade, one finds "a critical shift," a displacement of the traditional logic of state intervention in the economy based on the supply of goods and services in response to social and political considerations, with a new logic based on consumer demands. (295)

While governments and cultural industry spokespersons are increasingly justifying state support for culture by arguing the need to maintain cultural sovereignty and to create a market favourable to national cultural products, the authors argue for a different approach that emphasizes the importance of cultural development. (296) Cultural development is defined as "the process by which human beings acquire the individual and collective resources necessary to participate in public life." (292) As such, cultural development provides the resources that enable citizens to intervene socially, economically and politically. (296)

The view that commodifies culture "excludes and marginalizes all cultural practices that cannot be materialized in a market relationship, with the result that, for most people cultural activity becomes a socially neutered act of consumerism – one among many. Furthermore, placing a priority on industrial concerns means that cultural participation is increasingly a function of one's capacity to pay, thus extending existing social inequalities to the cultural sphere (Murdock, 1992)." (302-303) "The role of the state in this context is to redress the balance and see that democratic imperatives are not subordinated by industrial ones." (303)

The authors support a paradigmatic shift in emphasis in public policies, from cultural production to networks of distribution and points of consumption. They feel that emphasizing the principle of accessibility would foster a more active relationship between creators and users of cultural products. (310) This perspective of democratic cultural development would also require a broadening of the range of cultural institutions that enjoy public support, more social uses of new communications technology and a new look at media regulation as a means of ensuring equitable access to distribution markets for producers and consumers while continuing to meet public service objectives. (307)

> As we have seen, the principal justification for state intervention through cultural policy has, in most cases, focused on the need to promote national culture and national identity. Public policy should rather, in our view, seek to promote cultural development because it is essential to democratic public life. (310)

Richard Collins' paper, "Trading in Culture: The Role of Language in Cultural Development in an Open Economy," examines the impact of globalization on the ability of policy makers to achieve cultural goals. He considers why the imperatives of cultural and economic development are so often perceived as contradictory and examines the meaning of culture in the current context of globalization of economic activity. He also examines the importance of language as a factor explaining the structure of important cultural markets and the position of "new societies," such as Canada, in the global cultural economy. (1994: 377)

Collins notes that the development of an open economy and cultural free trade is often perceived as economically and socially damaging because it threatens the prosperity of information producers, the cultural levels of the population and the cohesion of society itself. (379) Recognizing that cultural exchange and trade in cultural goods has prevailed since Gutenberg's time, Collins suggests that what has changed is the pace of change and the acceleration of the dematerializing of cultural commodities. (383) Formerly, the main issue posed by the international circulation of culture was freedom of information, but now there are issues of economic interest and the desire of communities to assert their distinctiveness from other collectivities. "Thus...accelerations in the rate of cultural exchange and adulteration are profoundly troubling to societies based (as all must, to some extent, be) on common cultures and collective identities, and the reverse to societies based (as all must, to some extent, be) on universalistic and rational principles." (383)

Yet, as he notes, there are striking differences in how these problems have been addressed in "old" and "new" societies. (385) Although Canada is a subordinate and peripheral actor in the world's richest and most important information markets, its varied social composition makes it a microcosm of the world community and gives it links to other language communities and markets. These are not necessarily disadvantages. (395) Collins concludes that "It may be that 'new societies' such as Canada possess social structures and habits better fitted to the brokering roles increasingly required in an increasingly interdependent and internationalized world economy than do old-style nation states." (396)

As previously noted in *Vital Links* (1987), there is a need to join creators with their audiences if Canada's cultural industries are to flourish. Liss Jeffrey's paper, "Rethinking Audiences for Cultural Industries: Implications for Canadian Research," deals with some of the fundamental questions for researchers of Canadian audiences for the cultural industries within the context of international developments. She notes that in Canada, as elsewhere, conflicting assumptions about audiences underpin all aspects of cultural and economic development, including the appropriate limits of unregulated markets, the state's role in supporting cultural industries and producers, and the negotiations over the exclusion of cultural industries from international trade agreements. (1994: 496) She suggests that more focussed and refined audience research will help to clarify some of the conflicting values that animate trade disputes.

Two basic approaches to knowledge of audiences are outlined – the economic approach (market model), which defines audiences as consumers, and the cultural approach (public model), which defines audiences as composed of citizens. (496-498) Relevant considerations of the first approach include marketing concerns: product, price, placement and promotion. Those of the second approach include democratic values, education, public health and community safety, literacy and quality of community life. (496-498) As Jeffrey sees it, the main problem for advocates of the cultural approach is that cultural concerns are often qualitative – quantification is difficult but possible and not always meaningful. For example, how do you measure the effects of the repeated invasion of one culture's imagination, national identity and sovereignty by the mass media of another culture? (497-498) She feels that both quantitative and qualitative research is required to illuminate these matters and argues that neither element can be ignored if audience research is to contribute fully to debates over cultural and economic development. (498)

Her paper goes on to address six key themes that reflect a substantive rethinking of the nature and meaning of audiences: questioning of the validity of current audience measurement systems; inadequacy of our knowledge of what audiences actually do; fragmentation of mass audience due to increased choice; search for a distinctive calculus by public sector broadcasters; new research emphasizing the active nature of audiences; and examination of the fundamental assumptions animating debates over national identity and the impact of foreign broadcasters. (499-515) In addressing this last issue, Jeffrey notes that the Canadian case is of particular interest. Despite a highly advanced technological infrastructure, Canadian producers of English-language television programming have experienced repeated problems in reaching domestic audiences. (515) For Jeffrey, the key question is what sort of linkage exists between exposure to the media and cultural and national identity, particularly in a context where cultural consumption is not coercive. (514)

The paper concludes by briefly sketching the implications of the current rethinking of the nature of audiences for Canadian researchers. Jeffrey suggests that basic assumptions about both the "market" and "public" models need to be questioned, as do our assumptions about audience behaviour. Economic issues have dominated cultural industries research to the detriment of less measurable questions. "The programmatic call is for an audience model which carefully balances the claims and assumptions of market and public models. A clearer public calculus in which diversity is highlighted is urgently required, but this will not be fruitful in the absence of sustained attention to audiences as consumers." (518)

As the editors of the volume (McFadyen et al.) point out in their introduction, the central theme emerging from these papers is the tension between cultural objectives and commercial considerations:

> The inherent conflict between these two goals underlies much of what has occurred in the past in Canadian cultural industries research and policy-making. It will become even more important in the future as a result of the convergence of the broadcasting, telecommunications, and computer industries (popularly titled the "information highway"). (257)

In October 1997, culture and trade were again the central focus of a conference, organized by the Centre for Trade Policy and Law in Ottawa. The proceedings were later published as *The Culture/Trade Quandary: Canada's Policy Options*, edited by Dennis Browne. The conference dealt with four main themes: the social and economic rationale for domestic cultural policies; the impact of technology and technological change on our cultural industries; the treatment of cultural goods and services in international trade law; and the impact of globalization on culture and national identity. As Browne noted in his foreword, in recent years differences in perception between the Canadian cultural community and Canadian trade officials had driven a large wedge between the two communities. The conference was intended to bring them together for a frank and open discussion of the serious and increasing international challenges to Canadian policies. (1998: vii)

In his paper entitled "Social and Economic Rationales for Domestic Cultural Policies," Victor Rabinovitch (then Assistant Deputy Minister of Cultural Development in the Department of

Canadian Heritage) begins by illustrating the predominance of foreign content, mainly American, in Canada's cultural marketplace, citing the following statistics: 70 percent of music played on Canadian radio stations, 60 percent of all English-language television programming and 33 percent of French-language television programming, 70 percent of the Canadian book market, 83 percent of the newsstand market for magazines, 84 percent of retail sales of sound recordings, 95 percent of feature films screened in theatres, 86 percent of prime-time English-language drama and 75 percent of prime-time French-language drama. (1998: 30) He goes on to explain that the Canadian government has intervened in the cultural sector to achieve two fundamental objectives: "the development of cultural content and access to cultural content." (32) His concept of "cultural content" includes "categories of intellectual activities such as the reporting of news, information, analysis and debate, and the advancement of scholarship, as well as promotion of the performing, creative, and visual arts and entertainment." (32)

Quoting remarks made by the Minister of Canadian Heritage, Rabinovitch notes several observations flowing from recent experience in dealing with the emerging challenge of how to relate cultural objectives and trade and investment objectives:

1) A strong and viable domestic cultural base is the primary goal, and the Canadian market remains the primary audience for the products that are assisted through Canadian cultural policies.
2) Culture is not about the creation of a commodity or a service to be traded, promoted or invested in without regard for the sustainable diversity of cultural expression.
3) International trade agendas and regional economic co-operation agreements present major challenges to the survival of global cultural diversity.
4) Trade challenges are not the best way to examine the rationale for cultural policies and national cultural objectives.

5) Retaining a formal sovereign right to develop cultural policies is no longer adequate if program and structural measures put in place by a country are constantly assessed (or challenged against the standards set for trade in commodities or services}. (41-42)

Rabinovitch also makes the important point that while there are significant economic benefits from cultural activities in terms of direct employment, investment, tax revenues and indirect services, the fundamental impetus for cultural policy "is the need for identity, cohesion and avenues of expression that are part of the foundation of an enduring society." (38) He believes that Canada's cultural objectives are as important as foreign and trade policy considerations and that foreign policy is intended to be an extension or a projection of domestic policies and interests. (42)

In her presentation, "The Impact of Globalization and Technological Change on Culture and National Identity: A Call for Visionary Pragmatism," Liss Jeffrey contends that Canada should take a leading role in a multilateral effort to ensure the reversal of the trend to incorporate culture into economic trading regimes. (1998: 159) She views the cultural exemption in the FTA/NAFTA as an unwise trade-off, because existing rules are futile in resolving cultural industries disputes in international trading regimes. What is required, in her view, is a viable framework at the level of the nation-state to implement a counter strategy of "visionary pragmatism."

For Jeffrey, trade is not an end in itself, but the means to a higher quality of life. Culture – involving as it does the felt sense of a public communication space within which multiple identities can find a place – informs our civil values and makes possible our evolving democracy and quality of life. Within this vision, specific cultural, linguistic and racial communities can find room to grow and flourish with a distinctive Canadian framework for diversity with unity. (160)

> The wisdom of the Canadian position taken in the 1920s, and continued into the present through national ownership, regulatory, tax, and other policies, is that

> communications technologies and culture have always been linked to building national networks to ensure the nation's conversations. During the 1990s, cultural policy is shifting the agenda and this shift needs to take full account of the problems with the economic trading regime approach to culture, and the emergent digital media and multipath networking. The rationale is twofold: Canada should prepare itself for the digital convergence of the major Canadian cultural industries, telecommunications, broadcasting, and publishing; but, also, Canadians should continue to insist that their governments design a strategy that reflects their interest in ensuring access for all to a public communications space. (176)

Jeffrey concludes:

> Beyond keeping culture off the table, at the intersection of trade and cultural policy the most significant threat to Canada's communication space on the horizon will likely emerge from the difficulty in maintaining the separation of the cultural industries, which are ostensibly exempt from NAFTA, from the non-exempt telecommunications sector (Acheson and Maule 1996, 84-85). For the time being, Canada must insist that an operation that acts like a broadcast distribution undertaking, such as WebTV, be regulated under the Broadcasting Act. Otherwise, the ability to design policies to suit Canada's historical cultural aspirations will be abandoned by definition. (180)

In her paper, "The Impact of Technological Change on Canada's Cultural Industries," Sheridan Scott describes how the technological changes occurring in Canada's cultural industries are hastening the development of new media, namely interactive video, audio and text-based services rooted in the convergence of telecommunications, computing and broadcasting. These changes are also challenging traditional economic and regulatory models for the cultural industries and underline the need to develop new models to ensure that Canada continue to maintain and promote national sovereignty and to foster economic growth. (1998: 55) Citing the arrival of unauthorized, American-based direct-to-home services to Canadian customers and new media services carried over the Internet, she notes that as a result of technological change, geographical boundaries are increasingly less effective as regulatory points of control. (66-67) She also predicts that as new technologies lead to greater programming choices, there will be greater opportunities for content providers, and as content becomes more directly available to consumers, access will be controlled more and more by individuals than by regulators. Thus, she believes, a new approach for fostering Canadian content will have to be developed – one based more on promotion of Canadian content than on protection. (81-84)

Scott suggests that with the appropriate government policies aimed at encouraging and supporting new media, technology has the potential to very positively affect the development and distribution of Canadian cultural content. (83) However, she does not believe that using public policy to regulate the "cultural" growth of new media is the way. (82) Rather, she advocates a public policy economic intervention that would include a number of elements: continuing incentive and investment programs for traditional entertainment content such as the television production fund; encouraging conventional broadcasters to take advantage of digital production, quickly resolving issues surrounding digital transmission; not subjecting new media and Internet content to a traditional licensing regime, thus encouraging growth and enabling Canadian producers and distributors to take advantage of new economics of production and distribution; encouraging Canadian content developers and distributors to improve marketing of all types of Canadian programming; and encouraging the establishment of diverse funding sources for new media content aimed at fostering innovation in content and promoting synergies between creators of both traditional and interactive digital products. (84)

It is this "balance of current and new incentives, and a deregulatory approach to new media" that she believes "would appear to offer the best potential to encourage more production and more consumption of Canadian-produced content across the entire audiovisual spectrum." (84)

As Ivan Bernier remarks in the introduction to his paper, "Cultural Goods and Services in International Trade Law," the debate on Canada's cultural exemption has reached new levels of intensity. The purpose of his paper is to provide a general picture of the way cultural goods and services are currently treated in international trade agreements in order to facilitate the search for new directions. (1998: 111) After tracing the fundamental legal differences that exist between the treatment of goods and services, Bernier examines their treatment in the context of the WTO and NAFTA, under the investment provisions of the OECD, WTO and NAFTA, under bilateral investment agreements and finally under the intellectual property rights provisions of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) and NAFTA.

Bernier's survey of the various agreements demonstrates that there is still a great deal of ambivalence about the treatment of cultural goods and services, based on the fundamental question of the specificity of these goods and services. (146) Are they goods and services like any other, or should they be treated differently? Unfortunately, according to Bernier, there is no obvious answer:

> What is needed in reality is a twin-track approach that would recognize that cultural products, to the extent that they are traded, come under the ordinary rules of international trade agreements, but at the same time would make it possible for states to intervene in order to ensure a viable domestic cultural production and to favour better access to a diversified foreign cultural production. In other words, an approach that would distinguish between the industrial and the cultural objectives of government intervention. (147)

For Bernier, such an approach at the international level would not necessarily mean excluding cultural products from international trade agreements altogether, but rather would mean finding ways to permit derogation by signatory countries in defined circumstances, such as those used for general exceptions in the GATT 1994 and the General Agreement on Trade in Services (GATS), or for country-specific reservations such as in NAFTA. (147-148) Either way, Bernier feels that it is clear that the issue of treatment of cultural products in international trade will not go away:

> Canada, in that context, has a crucial role to play as the leading advocate of cultural exception clauses. Unless something like this is done, chances are that internationalization will win the day without even a serious debate on the issue, which would be too bad not only for the preservation of cultural diversity, but also for international trade itself. For diversity, including in a very fundamental way cultural diversity, is the essence of trade. (148)

In a 1997 monograph entitled *A Matter of Choice: Toward a More Creative Canadian Policy on Culture*, published by the C.D. Howe Institute, Daniel Schwanen examines Canada's current cultural policies in the context of further trade liberalization, the unfavourable WTO decision on Canadian measures to support the magazine industry as well as other pressures such as government budget constraints, Canada's growing international presence culturally and the rapid pace of technological change. In response to these pressures, he calls for a renewed focus on the objectives of Canada's cultural policy.

The underlying rationale for direct government intervention in support of culture, according to Schwanen, is the need to ensure that Canadians can share experiences and information about Canadians and Canada. However, he feels this direct intervention must be accompanied by steps that ensure a well-functioning market for cultural goods and services, including new copyright legislation that would ensure that creators receive a fair share of the benefits from the dissemination of their work and protection of the public interest. He also believes that the government has a continuing role to play in ensuring that foreign distributors of cultural products do not use market positions gained through economies of scale or vertical integration to shut Canadian products out of the market. (1997: 2)

Schwanen believes that the current definition of Canadian content used for tax, subsidy or broadcasting content rules should be focussed less on ownership and production expenditures and more on creative output and public interest. (2) He rejects the assumption that there is automatically a link between country of ownership of the distributor and the content of the product and suggests that investment rules need to be relaxed. Given the immense size of the "500 channel universe," the content requirements for broadcasting should be replaced over time with a policy ensuring shelf space for signals with high levels of Canadian content across a range of broadcasting technologies. (2) Noting that the WTO panel decision did not imply that Canadian and U.S. products were to be considered "like goods" in a general sense, he suggests that there is a wide range of measures Canada could still adopt to support the production and dissemination of domestic cultural content. Canada needs to obtain clarification through international negotiations on the extent to which subsidies and tax incentives can be used to promote domestic cultural products. (2)

Schwanen argues that our economic interests demand that we participate in freer global trade and investment "because a rules-based economic system actually works in favour of medium-sized economic powers such as Canada by, *inter alia*, permitting the market access negotiated among larger powers to be extended to all, and by establishing a dispute settlement mechanism that is reasonably immune from considerations of relative economic size between disputing parties." (4) These policies also need to be adapted to the new realities that have resulted from rapid technological innovations. (5)

> What is needed is a principled approach to policy in a wide range of cultural sectors, but flexible enough to permit policies to be tailored to fit specific market structures and technology in each sector, consistent with the overall approach. (6)

In her overview of culture and trade issues entitled *The Implications for the Cultural Sector of Harmonization of Economic Policies and Standards*, Rebecca Goldfarb reviews the body of academic literature that discusses harmonization and its implications for the cultural sector, particularly those implications arising from major international trade agreements such as the NAFTA, GATT, GATS and the now-defunct Multilateral Agreement on Investment (MAI) initiative. She defines harmonization as "the process whereby domestic economic policies are altered as a result of an increasingly integrated economic environment." (1998: 6) She divides the academic literature into two basic general frameworks: (1) the cultural view, which she further divides into the "cultural imperialist perspective" and the "nationalist viewpoint"; and (2) the economic view, which she divides into the "liberal economic perspective" and the "institutional perspective." The following is a brief summary of Goldfarb's characterization of these frameworks. (9-18)

The "cultural imperialist" variant of the "cultural view," which assumes the permanent dominance of culture emanating from the United States, traces its origins to Marxism, which sees mass communications as a "system of indoctrination and propaganda" and would characterize Canada as a "dependent capitalist state." From this perspective, much of the development of the cultural industries in Canada is about supporting the interests of American capital, not building a strong indigenous industry.

In contrast to the "imperialist" perspective, the "nationalist" perspective is not fundamentally about dependency but about culture as a tool for nation building, connecting "identity, sovereignty and unity to the production of domestic cultural products." (11) Nationalists generally express a concern that cultural industries in Canada have been more concerned with profit than with the creation of Canadian content. The problem, therefore, is less the result of American cultural imperialism than about conflicting domestic values. (13)

From the liberal economic perspective, while free markets and minimal state intervention are desirable, liberal economists generally do not oppose a role for government in the creation of culture, albeit a much more circumscribed role than the government currently plays in Canada. Goldfarb links the growing interest in minimizing state involvement in all sectors to a global trend that began in the 1980s, a trend that has been difficult to follow in Canada because of the long-held belief by "nationalists" that culture contributes to political stability and national unity. (15) The liberal economists question the link between culture and "cultural products" and make a clear distinction between harmonization of economic policies and harmonization of culture.

The "institutional" variant of the "economic view" sees Canadian policy as a combination of responding to the forces of globalization with free trade promotion and some form of cultural protection to achieve a desired level of Canadian content. From the institutional perspective, the current state of affairs, with a non-regime for culture, is untenable. Culture is assumed to be on the negotiating table. Institutionalists feel a rules-based system negotiated in international trade agreements (regimes and institutional) will ensure better trust, understanding, stability and security, ultimately making it easier for Canada to achieve its policy objectives in the cultural sector. (17)

Thus, it is not surprising that adherents of the cultural and economic perspectives found so much to disagree about in the FTA and to a lesser degree in the NAFTA. The utility of the cultural exemption, negotiated in this agreement under FTA Article 2005(1) and repeated in the NAFTA Annex 2106, has been the focus of much of the debate. Depending on one's perspective, the cultural exemption can be viewed as either irrelevant because the United Sates has the right to retaliate with "equivalent commercial effect" (19), or successful because it has never had to be used. (19-20)

From the economic perspective, non-use of the exemption is seen as evidence that "liberal institutionalism can allow for effective international rules and norms that will allow nations to maintain domestic policy choices." (20) Some liberal economists also suggest that the current mechanisms for protection, including the exemption, should be modified because the exemption creates a "misallocation of resources within Canada, enabling the government to play a role where it should not." (20) Others suggest that a rules-based trading system results in principles, norms and rules that are transparent and predictable rather than a regime that is neither transparent nor predictable. (20)

Goldfarb briefly discusses another issue emerging in the recent literature on the trade and culture debate – the determination of what is defined as a good and what is defined as a service – a distinction that is important because it determines whether GATT 1994 or the GATS will be applied in a particular instance. (22) Using the WTO ruling against Canada in the case of split-run magazines as an example, she points out that "the current rules, norms, principles and decision making procedures are somewhat uncertain, with respect to cultural goods, because services can be embedded in goods." (23)

Briefly turning to the question of subsidies in the cultural sector, Goldfarb suggests that if subsidies are not allowed or limited under trade regimes there is a danger that "cultural industries will become less able to promote a distinctly Canadian product." (23) She finds both economists and culturalists in general agreement that, if Canada chooses to protect culture, subsidies may be the best option. In terms of intellectual property, she notes a difference in the basis of copyright law in different trading partners. For example, economic rights have been the basis of copyright law in the United States, while moral rights form the basis for intellectual property rights in other countries. Thus, an exclusion of moral rights from the NAFTA and the WTO is seen by many as a further industrialization of culture. (24)

Goldfarb observes that debate during the discussions prior to the abandonment of the MAI replicated many of the same positions being taken prior to the signing of the FTA and focussed on what kind of exemption would be best – a self-designed cultural exemption as advocated by the French or a country-specific reservation favoured by Canada. Goldfarb believes a shift in outlook from the cultural to the economic has taken place. There appears to be a growing acceptance of both the reality and the benefits of global trade agreements. Thus, the focus of discussion has become more analytical and has shifted to the implications of specific conditions contained in the agreements. (26)

Much Ado about Culture: North American Trade Disputes, by Keith Acheson and Christopher Maule, is the latest major work (388 pages) to examine the differences in approach to culture in Canada and the United States and to trace the resulting conflicts in the context of technological developments as well as international agreements dealing with trade, investment, copyright, and labour movements. The nature of the Canadian cultural industries is examined, as are several cases of recent conflict. The authors also propose an alternative approach to the current cultural exemption in the FTA that would allow the gains from openness to be realized while responding to legitimate cultural concerns. In the interests of brevity, I will confine my summary of their views to the concluding chapter of the volume.

Briefly stated, Acheson and Maule argue that Canada's protectionist policies have been ineffective in changing American dominance of cultural industries. In their view, cultural industries are essentially international, and therefore protectionist policies make little economic sense, particularly for small countries (markets), because protection reduces wealth when producers are barred from the larger, dominant market. These policies have also failed in their objective to ensure more Canadian content. (1999: 331-333) They feel that both large and small countries need to achieve both access to and success in foreign markets in order to support their domestic production. "The best way to assist domestic industries, cultural and other, is to ensure that they are internationally competitive. The worst way is to condemn them to small domestic markets and to prop them up with subsidies." (334) While admitting that protectionist cultural policies are politically popular, Acheson and Maule predict that the popularity of these policies with voters will wane as dissonance increases between what is promised and what actually happens. (334) They also question public statements that emphasize American global dominance of cultural content, suggesting that a more appropriate description of the current situation would be "the dominance of the production and distribution of international content by a system that is also international." (335)

Acheson and Maule feel that the general acknowledgement that what we read, listen to, or watch matters does not justify policies that prohibit or make more expensive content based on criteria that do not relate to the content itself. Yes, Canadian voices are being subsidized and protected, but are Canadian stories being told? (335) In their opinion, the themes – "Americans against us," "the benefits of unspecified cross-subsidies," the "Canadian voices need a public space to tell Canadian stories" mantra and the "importance of ownership" – have been cultivated by a mix of interests – industrial, bureaucratic and political. (338) They predict that the willingness to pursue these policies will be reduced as access to foreign markets becomes more important than domestic protection and as the enforcement of protective barriers becomes more difficult; and that continuing with current cultural policies will result in retaliation and the stifling of exports, a major source of success for many cultural industries. They feel that this approach is unattractive to consumers and may also result in an exodus of talent. (338)

As an alternative approach to the current policy of protectionism, one that would allow the gains from openness to be realized while responding to legitimate cultural concerns, Acheson and Maule would draw on the examples of the special arrangements contained in international agreements dealing with other sectors such as agriculture, textiles, steel, aircraft, financial services, etc. Under these arrangements, individual goods have been conditioned by voluntary export and import restraints. (338) While they appear to resist freer trade, these special arrangements frequently prevent the introduction of further protectionist measures and include procedures that will lead to future liberalization. Acheson and Maule feel that such an arrangement for cultural industries could be designed to result in outcomes of mutual benefit. (339) Specifically, they favour a formal agreement that would include cultural and entertainment goods and services within the framework of the WTO with limited special provisions for particular circumstances, similar to the approach taken for telecommunication services, where a reference paper set out the definitions and principles for the sector's peculiarities. (346-347)

Developing such an agreement would require a number of steps:

- drawing the boundaries for the inclusion or exclusion of relevant activities in a way that would permit the impact of future technological development to be taken into account;
- determining the scope of the agreement with respect to trade in goods, services, investment, intellectual property, and the movement of persons;
- identifying factors affecting access by foreign firms to domestic markets;
- developing a list of subsidies and tax incentives affecting the industry;
- developing a list of private actions that affect trade, and identifying the scope of antitrust policy to deal with these policies from a trade policy perspective; and
- examining alternative dispute resolution procedures. (347)

They also suggest the following goals to which the sequence of commitments should aspire: no tariffs and quotas, minimal foreign ownership restrictions, non-discriminatory market access, freedom to work, co-ordinated enforcement of national antitrust laws, no direct or indirect protection of wholesale or distribution networks, national treatment in the application of censorship, national treatment of programming in "safe sanctuary" periods of the day, subsidies allowed to fill "gaps" in content, and national treatment in tax provisions and transparency. (347-348) They conclude by noting that even if a sectoral agreement is not the preferred route, these issues will still have to be addressed. (348)

A growing number of observers in the United States also question the current U.S. government approach to culture, as reflected in international trade negotiations, and are examining alternative approaches to deal with difficult trade/culture issues. For example, in a 1998 article, "Defending the Imaginary to Death? Free Trade, National Identity, and Canada's Cultural Preoccupation," Oliver J. Goodenough, like Carr (1991), traces the roots of the recurring Canada-U.S. friction over trade and culture to a conflict in ideals or "defining national myths" – the importance of protecting a national identity for Canadians versus the principles of free speech and free markets for U.S. citizens. (1998: 207) He feels that this makes it difficult for many Americans to step outside the parameters of their ideals to ask themselves whether protection and interference may be required to protect some things of social value. (206) He feels that Canadians, on the other hand, tend to ignore these underlying American ideals and see only the business aspects of the dispute. (207) He also notes that disputes are rarely over "high culture" (opera, ballet or the fine arts) or "ethnic culture" (folklore, traditional arts and architecture), but over "popular culture" – film, television, music, mass-market books and mass-market periodicals. (209)

In reviewing Canada's legal framework for the promotion and protection of its cultural autonomy, Goodenough observes a "certain schizophrenia" underlying both "strong" measures aimed at excluding U.S. products and weak ones ensuring choice, including: prohibitions, penalties and quotas on foreign products, investment regulation, the cultural industries exception in the FTA and NAFTA, its treatment under the GATT, and subsidies and incentives for Canadian cultural industries. (211) Faced with the recent discouraging rulings against Canada by the WTO, Goodenough feels that the pertinent question is "not about what the interaction of national and international law may be construed to require, but rather about what it should require." (222)

In making a case for the protection of culture, he explores four analytical arguments. (223-230) First, he suggests that cultures naturally defend themselves. "If the link between culture as 'product' and culture as 'value system' is indeed strong, then the theory of cultural transmissions may help to legitimize Canada's struggle. Cultural systems will generally contain self-protective responses against external forces of change. Therefore, the Canadian measures can at least claim to be implementing common, natural and perhaps necessary cultural and psychological tendencies." (223-224)

Second, he argues that the U.S. position as a model of free trade on cultural matters is flawed. (224-225) For example, U.S. broadcast television, radio and newspaper ownership restrictions limit foreign interests to not more than 20 percent, using the rationale of national security. (224) Third, he asserts that a great deal of U.S. cultural production exploits emotional manipulation for the purpose of creating further paying demand for more of the same. Therefore, "the popularity of United States cultural product is not just the result of economies of scale, or the dominance of the English language internationally, although these are not trivial elements. The U.S. product is also popular because it is made by an industry which values popularity, and which under the legal regime of its native land has the creative license to pursue popularity, with very few legally-imposed constraints promoting a 'better' diet." (226-227) He suggests that "Canada's measures to counteract a drivel infestation are almost all *origin* driven and *content* neutral...Nonetheless, if content is the concern, *geographic source* restrictions are at best an oblique way to pursue it." (227)

Finally, he argues that "free trade principles must be sacrificed in some contexts to help preserve the societal underpinnings on which the possibility of free trade ultimately depends." (223) There are costs to maintaining a civil society, and cultural protectionism is one of them. At the same time, Goodenough wonders if Canada's cultural protection policy really does what it claims to do and suggests, "If exclusion is the goal, most of the measures do not currently work, and this failure will likely get worse; if choice is desired, the measures largely exclude a prime potential source of choice: American-owned but Canadian-oriented products." (230)

Goodenough also suggests that exclusionary prohibitions of U.S. cultural products can in some ways be viewed as undemocratic and highly suspect because they suggest that Canadians cannot be trusted to make the right choice in the popular culture they consume. (235) He believes that the real divide is between the two realms of culture (high culture versus popular culture) and not between the United States and Canada. "Supporting these endeavours [opera, ballet, novels and fine arts] with public money may be a good idea. Limiting access to the Disney Channel, however, will have little impact on the strength of Canada's high culture institutions and artists, although such a limitation is likely, over time, to weaken the popular appeal of Canadian animation." (237)

While accepting that there are different ways that Canadians and Americans view many aspects of the world, and that there is good empirical evidence that there are distinctive Canadian attitudinal traits whose strength is increasing, he wonders if protectionism is irrelevant because, at the level of popular creative works, there is such a great deal of sharing across English-speaking North America. (239) Citing cultural transmissions theory, he suggests that "most foreign influences will 'bounce off' a healthy culture without government intervention, or at the very least will be compartmentalized for use in contexts separate from hearth and home. Where the link between exposure to foreign product and a change in domestic values is weak, there is little to worry about. On the other hand, the penetrating ability of those that do not 'bounce off' will be little affected by government-level efforts to keep them under quota." (241)

In the concluding section of his paper, he suggests it is time for a "new strategy built around subsidies and constructive engagement with the United States." (247) Rather than fighting Hollywood, Canadian policy should be to look for ways to work with it. "Xenophobia and strong protectionism on the ownership front may well be getting in the way of making popular and widely-seen Canadian content films and television programming. When it subsidizes Canadian owners rather than Canadian product, weak protection does not work either." (247)

Writing in *Business Week* (November 1998), Jeffrey E. Garten, Dean of the Yale School of Management, calls on the government and on corporate America to lessen U.S. cultural dominance by encouraging cultural diversity around the globe. He urges the U.S. government to reverse current trade policy and permit temporary quotas and subsidies abroad to preserve certain local cultural industries. He also urges multinational corporations themselves to fund native entrepreneurs wishing to create cultural industries, to showcase regional film and theatrical productions and to finance university research and teaching of history, art and literature. (1998: 26)

He concludes his article with this warning: "Protecting national cultures could soon become a defensive rallying point for societies buffeted by globalization and undergoing tumultuous change. Being more sensitive to foreign concerns would ease the prospect of back lash and even bolster America's ability to export its ideas and ideals for the long haul." (26)

Economic Integration – Culture and Identity

As mentioned previously, cultural industries are the means of communication, the conduit to the Canadian public, for the cultural goods and services produced by Canadians about Canada. The direct impact that freer trade has on the well-being of this sector of the economy has a secondary impact on the distinct Canadian identity it is meant to create, support, preserve and protect. This leads our discussion to a second set of questions about trade and culture: Is trade having an impact on national identities? How different are our values from those of our major trading partner? Is trade liberalization affecting the legitimacy of the nation-state as a repository of distinctive, common cultural values?

In his comparative study, *Continental Divide: Values and Institutions of the United States and Canada*, Seymour Martin Lipset notes that, despite the development of both countries into industrialized, wealthy, urbanized and ethnically diverse societies, the dissimilarities, particularly the cultural differences, of the past continue. "To reiterate an analogy, the two are like trains that have moved thousands of miles along parallel railways tracks. They are far from where they started, but they are still separated." (1991: 212)

Lipset feels that despite trade liberalization Canadian values have survived what is already an American-dominated mass cultural market. "Given modern means of communication, the diffusion of mass media, and easy travel, the tenacity of cultures – their ability to hold on within merged economies and polities – is amazing." (221-222) Lipset also believes that the cultural and political differences between the two nations help to explain their occasional difficulty in understanding each other in the international arena. (220) "Americans, more than other western peoples, tend to view international politics in non-negotiable moralistic and ideological terms. Canadians, like Europeans, are more disposed to perceive international conflicts as reflections of interest differences and, therefore, subject to negotiation and compromise." (220)

Lipset goes on to note that perhaps the most important step that Canada has taken to Americanize itself – far greater in its implications than the signing of the free trade treaty – has been the incorporation into its Constitution of the Charter of Rights and Freedoms, which places the power of the state under judicial restraint. (225)

In a more recent discussion of North American values, *The North American Trajectory: Cultural, Economic, and Political Ties Among the United States, Canada, and Mexico*, Ronald F. Inglehart, Neil Nevitte and Miguel Basanez examine how changes in basic values in the United States, Canada and Mexico are transforming economic, social and political life, resulting in an increasingly compatible cultural perspective among them. Their findings were based on a comparison of cross-national surveys carried out in 1981 and 1990. They observe that, generally speaking, as old economic boundaries are becoming eroded, a narrow 19th-century nationalism is gradually giving way to a more cosmopolitan sense of identity. (1996: 1-2) The authors feel that these changes are rooted in long-term generational differences and for this reason they will probably endure, and their cumulative effects will likely be massive. (167)

One of their concerns is the interplay between economic forces and human values. They feel that economic prosperity is an instrumental goal, not an end in itself. They note that "Free trade is a hotly debated issue not just because it leads to redistributive economic conflicts but also because it brings into play dilemmas grounded in the tension between two imperatives: the drive to attain economic prosperity through maximizing economic efficiency, and the drive to achieve noneconomic human goals. Economic welfare is one horn of the dilemma, with a nation's status and autonomy being the other." (35) In Canada, free trade with the United States is controversial because Canadian and American national values seem so similar that Canadian identity is threatened. Canada has a fragile national consensus, one fractured by historical linguistic, cultural and regional divisions and further aggravated by contemporary political disputes about how those cleavages should be constitutionally managed. (35) Yet, as noted in this survey of public attitudes to freer trade in all three countries, Canadians and Mexicans are clearly more eager for freer trade than are Americans themselves. (44)

While the authors do not suggest that political union is imminent, "One provocative implication that flows from these findings is that the traditional, historically entrenched rationale for the existence of political borders separating the three North American countries seems to be eroding." (171) However, citing the examples of Canada, Switzerland and the Soviet Union, they find little evidence that doing away with political borders will mean the disappearance of cultural differences. (171) They also question the assumption that comprehensive free trade will result in the standardization of public policies. As their findings indicate, a clear majority of citizens in all three countries want publicly funded health care – thus, they anticipate a policy harmonization away from and not toward the current American standards. (171) Contrary to some fears expressed during the negotiation of the NAFTA, they do not find any evidence that the Mexican public is more likely to sacrifice environmental standards for economic prosperity, even if this has not automatically translated into public policy. (171)

Their study suggests that some of the most basic values of the United States, Canada and Mexico are gradually changing – on a common trajectory, moving in the same direction, but not converging toward a common model, which is the United States. Indeed, in many respects Canada is ahead of the United States, though moving in the same direction. (81) What they feel is happening is not the Americanization of North America, but a common response to global forces. This process is frequently misperceived as Americanization simply because the United States is the mass media centre of the world, and the symptoms of change are often detected and publicized first in the United States. In reality the three societies are converging toward a model that none of them has yet attained. (162) "What we seem to be witnessing is neither divergence nor

Americanization, but a complex process of modernization that is changing all three societies in a broadly similar fashion." (81)

Michael Adams comes to similar conclusions in *Sex in the Snow: Canadian Social Values at the End of the Millennium* (1997). Using annual survey data on social values gathered by Environics Research since 1983, Adams uses a multivariate clustering and mapping technique to plot psychographic stereotypes or groups on a two-dimensional grid: (1) individual versus social inclinations; and (2) traditional versus modern values. The result is a "psychographic geography of Canada" that aims to portray the diversity of the Canadian character.

In comparing Canadian values data with those for the United States, Adams asserts that the "socio-cultural differences between Canada and the United States, like the differences between Quebec and the rest of Canada, or even between men and women, may be diminishing over time, but the differences that remain will…be significant and meaningful for many generations to come." (178) In his opinion, "although economic integration continues apace, there has been much less socio-cultural assimilation of Canada by the United States than is often feared. In important ways Canadians and Americans live different sorts of lives. Moreover…such assimilation will not take place for many generations to come, if ever." (194) He finds that French Canadians and English Canadians have more in common with each other than either group has with Americans. "And in spite of our growing intimacy with American commerce and culture, Canada remains a distinct society on the northern half of the North American continent." (195)

A less sanguine view of the threat to national identities posed by economic integration has been taken by many European commentators who see the Americanization of the world's culture as a clear and present danger. One particularly outspoken opponent of this perceived threat is Ignacio Ramonet, editor-in-chief of the journal *Le Monde Diplomatique*, who has collected a series of his essays on globalization together in one volume entitled *Geopolitics of Chaos* (translated from the French by Andrea Lyn Sacara).

According to Ramonet, Europe is confronted by three serious crises: an economic crisis, a demographic crisis and a cultural crisis. (1998: 142) He notes that since 1954, when European television became a reality, Europe has been inundated with American mass culture. "A new civilization took shape whose matrix, developed in the United States, is – for the first time in two millennia – foreign to Europe." (145) He feels that increasing globalization of the economy and of culture has further blurred the national framework. Stripped of essential cultural reference marks, and having lost their identity, people are facing the current crisis under the worst mental conditions. (137-138) Furthermore, "the logic of the market, free trade and the search for maximum profit, are threatening the cultural and creative domains." (149) In this respect, he finds WTO negotiations that include fields related to cultural production – audiovisual and cinematographic sectors – disquieting. (149)

While acknowledging that new technologies offer great creative opportunities, Ramonet fears that the United States' quasi-absolute domination of these technologies may lead to new forms of dependence and a condition of cultural vassalage. "World culture – in English – is spreading on a planetary scale and is imposing itself everywhere, not only in the countries of the South, but also in Europe." (154) Freedom of expression is being set in direct competition with the "freedom of commercial expression," which is sometimes presented as a new "human right." (158) "The doctrine of globalization equates freedom, plain and simple, with the freedom to do business." (158) The central idea in this new doctrine is expressed in roughly these terms: "Let people look at what they want to. Leave them free to enjoy. Trust their common sense. The only sanction applied on a cultural product must be its failure or its success in the market." (159)

For Ramonet, the final result of globalization of the economy, "preventable but already palpably present, is a combination of three dynamics that are converging explosively upon humanity at the end of this century. They are: globalization of the economy, the ultimate avatar of Western modernity, dating from Europe's world-wide expansion in the 15th century; reducing the role of the State – which may ring the death knell of politics and civil society all together; and the generalized destruction of cultures, North and South alike, by the steamroller of communications, mercantilization and technology." (58)

Economic Integration – Social Disintegration?

In addition to the fear that cultural identities are threatened by economic globalization, a growing number of observers are expressing concern that the integration of economies around the world is leading to increasing pressures on the "social contracts" that hold these societies together. Some critics see international trade agreements as creating more social inequality in our society and posing a threat to basic social policies, programs and solidarity. This leads us to a third set of questions about trade and culture: What are some of the short and long-term impacts of trade liberalization on social cohesion? What role can the state play in preserving social cohesion in the context of a global economy?

As the recent report of the Senate Committee on Social Affairs, Science and Technology, *On Social Cohesion*, indicates, governments and business are under pressure to start thinking more about the longer-term societal implications of economic policies such as trade liberalization. The key question posed by the committee was: "What forces will hold Canadian society together in an environment shaped by intense global competition and fast-moving technological change?" (1999: 2)

The report cautions that "for many in government and in the business world, the standard approach to globalization is to emphasize the benefits of the free flow of goods and capital, and to overlook the social fallout that may result. For too long, we have assumed that short-term social costs could be offset against long-term economic gains. What we forgot to take into account was that social damage could itself frustrate economic objectives." (10) The report also warns that the political consensus in favour of policies designed to enhance economic efficiency and growth could easily evaporate if the sacrifices and social costs are seen to fall primarily on the poorest and weakest segments of society, and the benefits are enjoyed by others. Unless they feel some stake in economic growth, they are likely to withdraw their support for free trade, capital mobility, relatively open immigration, deregulation and other similar features of open economies. (9-10)

The Senate committee observed that for many Canadians, globalization is exposing social fissures between those with the education, skills and mobility to flourish in an unfettered world market – the apparent "winners" – and those without. Social disintegration is not inherent in globalization. However, since liberalization exposes domestic producers to volatile global markets and to capital flows that are large relative to the economy, it increases risks – but it also increases potential rewards. For social cohesion, the challenge is to identify policies that enable those left behind to participate in markets on more equitable terms, nationally and globally. (10)

The report notes that until recently, most experts and policy makers in government believed that there was a trade-off between social and economic issues, between social justice and economic performance, between market and society. The report cites recent evidence from international research demonstrating that more equal societies are likely to be more prosperous in the long term and to have higher levels of well-being. (10) Equality has a positive impact on investment, both in human capital and in physical capital. (12)

The report's authors feel that the rise of transnational corporations has delivered "a significant blow to social cohesion and to the post-war social consensus." (17)

> Ownership of such corporations is increasingly spread among several nations, and the various components of

> major products are each produced in different countries. They operate on a world-wide or global footing. They have no nationality and are not rooted in any local or national communities. Today, in the new global economy, corporations and those who manage them are not as economically dependent on the local or regional economy as they once were, and thus have less self-interest in insuring the well-being of citizens. (17)

The report also makes the point that markets are social institutions, and their continued existence is predicated on the perception that their processes and outcomes are legitimate. Because the international or global market is the only market that is not regulated by an overarching political authority, transactions undertaken in the global marketplace carry the least inherent legitimacy, thus creating an important source of tension between globalization and society. (30) Institutions lacking legitimacy do not function well in the long term. Markets are no different. Therefore, making globalization more responsible means ensuring that the global market operates according to a certain set of rules and institutions that a majority of people see as being legitimate. (36)

In summary, the Senate report contains three key messages:

1) The most serious challenge for decision makers is to ensure that economic integration driven by globalizing markets does not lead to domestic social disintegration.
2) Social cohesion is about shared values, but it is also about redistributional issues.
3) Canadians have choices to make in addressing the socio-economic challenges posed by globalization and technology. (2)

Some academic research and thinking supports the kinds of concerns expressed in the Senate report. A recent National Bureau of Economic Research study by Alberto Alesina, Enrico Spolare and Romain Wacziary, entitled *Economic Integration and Political Disintegration,* links trade liberalization with political separatism. The paper provides a formal model of the relationship between openness and the equilibrium number and size of countries, and then tests the implications of this model by tracing the process of country formation and succession from the 19th-century formation of nation-states through to the present day. (1997: 18-26)

The findings suggest that in a world of trade restrictions large countries enjoy economic benefits because political boundaries determine the size of the market; therefore, in a world of free trade and global markets, relatively small cultural, linguistic or ethnic groups can benefit from forming small and homogeneous political units that are economically integrated with others. While the authors recognize that national borders still matter, their study implies that, as the process of economic globalization progresses, the trend of political separatism will continue. (25-26) "The concept of relatively large and centralized nation-states is and will be more and more threatened by regional separatism from below, and the growth of supranational institutions from above, in a world of 'global' markets." (27)

Harvard economist Dani Rodrik has examined issues related to globalization, economic integration and social conflict in a number of papers, most notably in his 1997 book entitled *Has Globalization Gone Too Far?* In addressing this issue, Rodrik argues that "the most serious challenge for the world economy in the years ahead lies in making globalization compatible with domestic social and political stability – or to put it even more directly, in ensuring that international economic integration does not contribute to social disintegration." (1997: 2)

Rodrik identifies three major sources of tension between the global market and social stability caused by economic integration. First, he points out that globalization may result in increasing asymmetry between groups that can cross national borders and those that cannot (owners of capital, skilled workers and professionals versus unskilled and semi-skilled workers and middle managers). Thus, unskilled workers in one country may find themselves more easily replaced by workers in other countries. (26) Second, globalization engenders conflicts within and between nations over domestic norms and social institutions that embody them (e.g. workplace practices, legal rules, social safety nets, and labour and environmental standards). This occurs because differences in national social arrangements have implications for trade and investment flows and, in turn, these flows impinge on national social arrangements. (48) Third, globalization has made it exceedingly difficult to provide social insurance. (4-7) He feels that the problem stems from globalization placing increased demands on the state to provide social insurance while, at the same time, reducing its ability to perform this role effectively and, thus, endangering the social consensus required to keep domestic markets open to international trade. (53)

Rodrik does not believe that globalization has gone too far, but he cautions that, if handled badly, the social pressures resulting from global economic integration will result in "bad economics" and "bad government," not only because it will exacerbate tensions between groups, but also because it will reduce the willingness of internationally mobile groups to co-operate with one another in resolving their differences. (70) Globalization "delivers a double blow to social cohesion – first by exacerbating conflict over fundamental beliefs regarding social organization and second by weakening the forces that would normally militate for the resolution of these conflicts through national debate and deliberation." (70) In conclusion, Rodrik reminds us, "The broader challenge of the 21st century is to engineer a new balance between market and society, one that will continue to unleash the energies of private entrepreneurship without eroding the social basis of cooperation." (85)

Just before the WTO meetings in Seattle in the fall of 1999, Dani Rodrik wrote an op-ed article entitled "Five Simple Principles for World Trade." As Rodrik states, "All sides in this acrimonious debate agree that the stability of the international economic system is predicated on a system of global rules. What is contested is the nature of these rules." Rodrik goes on to suggest the principles on which all sides should agree:

- Trade is a means to an end, not an end in itself.

- Trade rules have to allow for diversity in national institutions and standards.
- Non-democratic countries cannot count on the same trade privileges as democratic ones.
- Countries have the right to protect their own social arrangements and institutions.
- But they do not have the right to impose their institutional preferences on others.

In his recent book, *The Lexis and the Olive Tree*, American journalist Thomas L. Friedman also illustrates some of the complex issues relating to globalization, including the impact of globalization on culture, by providing examples from his own first-hand observations of what can happen when societies and the forces of globalization collide. He observes: "When you strip people's homes of their distinctiveness – either by homogenizing them or by destroying them environmentally – you undermine not only their culture but also social cohesion. Culture, at its best, can be one of the most powerful forms of voluntary restraint in human behaviour. It gives life structure and meaning. It sanctions a whole set of habits, behavioural restraints, expectations and traditions that pattern life and hold societies together at their core. When unrestrained globalization uproots cultures and environments, it destroys the necessary underlying fabric of communal life." (1999: 242)

Friedman also believes that the forces of globalization are contributing to the "widespread feeling, particularly within democracies, that even if people have a democracy at home they have lost control over their lives, because even their elected representatives have to bow now to unelected market dictators." (161) Because globalization is creating a single marketplace – with huge economies of scale that reward doing the same business or selling the same product all over the world all at once – it can homogenize consumption simultaneously all over the world. And because globalization as a culturally homogenizing and environment-devouring force is coming on so fast, there is a real danger that in just a few decades it could wipe out the ecological and cultural diversity that took millions of years of human and biological evolution to produce. (221) The greater discrepancy between a country's cultural norms and the norms of the globalization system, the more wrenching will be the process of adapting to it. (335)

Friedman suggests that one way to mitigate these effects is to practise sustainable globalization. "You cannot build an emerging society – which is so essential for dealing with the globalization system – if you are simultaneously destroying the cultural foundations that cement your society and give it the self-confidence and cohesion to interact properly with the world...My concern is that without sustainable environment there is no sustainable culture and without sustainable culture there is no sustainable community and without a sustainable community the is no sustainable globalization." (243) In a sense, the biggest threat to globalization today is globalization itself. (332)

In a recent address to the Industry Canada Distinguished Speakers in Economics Program, "What's a Country For? Globalization, North American Integration and Social Policy," Keith Banting expressed the view that the evolution of social policy has been shaped by the dual role of the state – domestic and international. (2000: 1) He poses the following questions: "Is it possible to engage fully in the global economy, and still preserve a distinctive national approach to the social contract? Or are competitive economic pressures narrowing the degrees of freedom enjoyed by the state? Are advanced democracies converging on a transnational model of social policy? If this is the case...What's a country for?" (1)

Banting concludes that predictions of an inevitable convergence of social policy regimes are not sustained by the evidence. (5-6) Taking, for example, social spending as a proportion of gross domestic product for OECD countries, he found that convergence was actually stronger in the 1960s and 1970s than it is today. (6) This is not to say that economic integration is irrelevant; however, the overall evidence suggests that the pressures for harmonization or a "race to the bottom" are not overwhelming. (7) Banting believes that while the constraints are real, they do not represent economic determinism. There is important room for national variations around the common themes of modern life. The extent of convergence between Canadian and U.S. social regimes will depend as much on the evolution of domestic politics as economic imperatives. We need to find ways of re-embedding economic liberalism in a system of social protection adapted to a new century. This will require a return to the language of social rights, although in a form suited to a global era. (13). "What's a country for? It seems that part of the answer remains that it is an instrument for reflecting distinctive domestic cultures and politics." (7-8)

Trade, Culture and the International Cultural Community

As early as the publication of the *Report of the McBride Commission* (International Commission for the Study of Communications Problems) in 1980, UNESCO recognized that intervention was required to achieve a more just and equitable balance in the information flow and cultural expression between larger, wealthier countries and those smaller and less developed. More recently, in 1995, the World Commission on Culture and Development submitted a report entitled *Our Creative Diversity* to UNESCO and the United Nations. This 300-page policy-oriented report explores the "two-way relationship between culture and development." Development, more than just economic growth, is defined as "a process that enhances the effective freedom of people involved to pursue whatever they have reason to value." (1995: 14) Culture is defined as "ways of living together." (14)

The Commission sees culture as more than just an instrument of economic growth, but also as a desirable end in itself. The report notes that the growing economic importance of cultural industries has created a tension between commercial interests and the desire for content that reflects diversity. The report urges a rethinking of cultural policies, suggesting that governments take a less direct, more facilitating role both in promoting cultural products and also in correcting some of the distorting effects of free market mechanisms. (41) Central to the report is its International Agenda for Culture and Development. A theme that is woven throughout its recommendations is the need for national governments and actors and international agencies and bodies to work together to promote cultural diversity.

In 1998, as a follow-up to *Our Creative Diversity*, UNESCO published the first World Culture Report, *Culture, Creativity and Markets,* as part of the UNESCO World Report Series. This interdisciplinary collection of the work of economists, social scientists, anthropologists and other specialists provides a broad range of hard data on the subject of culture and development viewed within the wider context of globalization. The analysis throughout the report demonstrates that culture is not only concerned with artistic creation and ethnic and indigenous issues, but also has social and political dimensions. (1998: 345)

Of particular interest to the discussion of issues related to trade and culture is Part 3 of the report, *Creativity, Markets and Cultural Policies*. The research outlined in this section of the report raises questions about how societies can best manage the impacts of globalization on local and national cultures and their creativity in order to sustain, preserve and protect them, and examines ways that cultural policy can be reconceptualized and reformulated to meet these changing demands. (154) The report cautions against counterproductive, inward-looking and defensive responses to global economic change and favours positive approaches that look at new opportunities to harness change and manage it. (156) It deals with several key aspects of cultural policy: the impact of global markets on creativity, on the emergence and development of cultural industries, and on cultural heritage; and protection of the rights of creators and the public interest in the age of cyber-culture. The research also suggests that many cultures and cultural products are stimulated by intercultural contact and global markets rather than being threatened by them. (156)

The report calls for a recasting of cultural policies so that the positive impact of globalization on creativity, its opening up of markets, can be identified and encouraged; and calls for recognition of the positive and negative impacts of global markets on cultural industries "so that policy can protect and enhance their cultural and economic flowering." (345) Although it argues that diversity contributes to creativity, the report acknowledges that it is not enough simply to advocate diversity in the abstract. *Our Creative Diversity* "sets the scene, but our task now is to go beyond this and show precisely how diversity enhances economic success, social opportunity, political stability and conflict resolution, besides being valuable, beautiful and delightful in itself." (343)

Canada has been working very actively with other countries to promote the idea of cultural diversity in a number of international forums, at both the ministerial and officials level. International discussions have been particularly active in the last two years, during which a series of meetings have been organized by international organizations such as UNESCO, the World Bank and the Council of Europe to provide the opportunity for country representatives to share views and experiences on how best to protect and promote cultural diversity.

For example, in February 1998, a roundtable colloquium, Canada and the Council of Europe: A New Partnership, was hosted by the Canada-Europe Parliamentary Association. As noted by the roundtable participants in the ensuing report, increasing economic integration brings with it interpenetration of languages and cultures. The challenge of preserving social cohesion while coping with economic change has become a global phenomenon. "For advanced liberal-democracies in Europe, as in Canada, the challenge arising from these globalizing forces is to take advantage of the economic, social and cultural benefits that new technology and open markets offer, while minimizing or eliminating the clear dangers they also present." (1998: 6)

As governments have been compelled to deal with a wide range of economic exigencies, citizens have felt the effects of government cutbacks across the broad spectrum of social policy areas including education, health, social services and housing. (8) Because culture mirrors a society's history and identity, it is essential for the development and expression of its values as well as for developing trade, employment and tourism. This is why governments have traditionally taken important measures (legislation, policy and programs) to support culture. Pressures from international trade agreements to liberalize trade and investment have also strengthened some governments' will to promote protect and preserve all aspects of cultural life in their countries, partly in response to the pervasiveness of American popular culture, and as a result of difficulties encountered when trying to preserve the ability to protect culture when negotiating new trade and investment agreements. (7)

As one conference presenter, Canadian author John Ralston Saul, put it, "Stop thinking and acting as though globalization were inevitable; adopting a passive attitude leads to accepting its repercussions. If human beings are intelligent enough to create new technology, why are they not intelligent enough to direct it instead of being directed by it? It is unacceptable that the fate of social programs, education and culture should be determined on such economic grounds." (30) Saul urges that culture and education not become "discretionary commodities." They are fundamental to society and should not be treated in simplistic market-exchange terms like a good or a service. (30-32)

Taking as a point of departure the 1995 report *Our Creative Diversity*, UNESCO held the Intergovernmental Conference on Cultural Policies for Development in Stockholm, Sweden, in March-April 1998. As a result of its discussions, the Stockholm conference adopted an Action Plan on Cultural Policies for Development, which reaffirms the fundamental principles of the

1982 Mexico City Declaration on Cultural Policies, stressing "that in its widest sense, culture may now be said to be the whole complex of distinctive spiritual, material, intellectual and emotional features that characterize a society or social group." (1998: 1) By definition, culture "includes not only the arts and letters, but also modes of life, the fundamental rights of the human being, value systems, traditions and beliefs". (1) The action plan also stresses the cultural dimension of development and the need to recognize the importance of universal values as well as cultural diversity. It highlights the growing importance of civil society in the field of culture and the importance of ensuring scope for the flourishing of creative capacities. Recognizing the rapid pace of social, technological and cultural change and the growing disparities at the national and international level, the plan underlines the importance of respecting intellectual property rights in view of the risks and challenges arising from the promotion of cultural industries and trade in cultural products.

In June 1998, on the heels of the Stockholm meeting, the Minister of Canadian Heritage hosted a conference in Ottawa dealing with international cultural policy and the importance of sustaining local and national cultures in an increasingly globalized world. The discussions focussed on three major themes: cultural diversity and development, the role of culture in global relations, and culture and trade. This last theme further examined a key conclusion from the Stockholm conference, namely that cultural goods and services should be fully recognized and treated as being not like other forms of merchandise. (1999: 14-17) Discussion also focussed on how best to build bridges between cultural and economic interests and develop strategies for the private and public sectors, and for non-governmental and international organizations. The conference resulted in the launching of an International Network on Cultural Policy, currently composed of ministers from 38 countries, whose purpose is to build increased awareness and support for cultural diversity in an era of globalization and technological change. The network continues to work toward this aim at both the ministerial and officials levels through a series of formal and informal meetings and workshops.

Canada continues to take a leadership role in promoting cultural diversity internationally. The discussions in Stockholm and Ottawa have been accompanied by meetings in Paris, Rio de Janeiro, Washington, Rome and Oaxaca. There have also been joint declarations with the governments of Mexico and France in support of cultural diversity. The Department of Foreign Affairs and International Trade and the Department of Canadian Heritage continue to work with stakeholders at home and with governments and international organizations abroad to promote and apply Canada's vision of cultural diversity.

New Strategies for Canadian Culture and Trade

The Cultural Industries Sectoral Advisory Group on International Trade (SAGIT) is part of the federal government's advisory system on international trade. It provides a means for officials from the Department of Foreign Affairs and International Trade and the Department of Canadian Heritage to consult with representatives of Canada's cultural industries. In February 1999, the SAGIT released a position paper, *New Strategies for Culture and Trade: Canadian Culture in a Global World,* which expresses concern over the effect that global trade, combined with rapid technological change, is having on our ability to promote Canadian culture. The report outlines a number of pressures for change that are creating both challenges and opportunities for Canada's cultural industries:

1) Digitization and the convergence of the broadcasting, cable, satellite and telecommunications sectors are creating new technologies, which will compete with existing distribution systems. At the same time, there will be even greater opportunity to distribute Canadian content both at home and abroad.

2) Emerging technologies are offering Canadians new communications tools but are also challenging the government's ability to enforce regulations designed to ensure that Canadians have access to Canadian cultural products. (Note: throughout the paper "cultural products" refers to both goods and services.)
3) With the growth of multinational corporations and the vertical integration of entertainment, distribution and delivery systems and products, national policies are shifting and adapting to address these changes.
4) The trend to more open markets and a free trading world makes it more challenging to negotiate trade agreements that recognize cultural diversity and the unique nature of cultural products. (1999: ii)

The report describes the cultural policies now in place in Canada, cultural policies used by other countries, and the growing pressure from technology and international trade agreements. It then sets out options for Canada's cultural trade policy. The SAGIT proposes that Canada reaffirm the importance of cultural diversity and the desirability of ensuring that a country's own stories and experiences are available both to its citizens and to the rest of the world. In the SAGIT's view, there are two main approaches:

1) the cultural exemption strategy used in the past, which takes culture "off the table" in international trade negotiations; and
2) a new strategy involving the negotiation of a new international instrument that would specifically address cultural diversity and acknowledge the legitimate role of domestic cultural policies in ensuring cultural diversity. (ii)

According to the SAGIT's analysis, there is growing concern worldwide about the impact that international trade and investment agreements are having on culture and a recognition that the tools and approaches used in the past to keep cultural goods and services from being subjected to the same treatment as other goods and services may no longer be enough, that the cultural exemption approach has its limits. Outlining a number of trade challenges to Canadian cultural policies that have taken place recently, the SAGIT report points out that, as countries develop freer trade, disciplines may become stricter and the number of challenges to domestic cultural policies could increase. (26) These challenges highlight the need to foster an environment where cultural expression and diversity can thrive. The report proposes that Canada call on other countries to develop a new international cultural instrument that would acknowledge the importance of cultural diversity and address the cultural policies designed to promote and protect that diversity. This new international instrument would:

- recognize the importance of cultural diversity;
- acknowledge that cultural goods and services are significantly different from other products;
- acknowledge that domestic measures and policies intended to ensure access to a variety of indigenous cultural products are significantly different from other policies;
- set out rules on the kind of domestic regulatory and other measures that countries can and cannot use to enhance cultural and linguistic diversity; and
- establish how trade disciplines would apply or not apply to cultural measures that meet the agreed upon rules. (32)

Recently, in a speech delivered to a symposium held at New York University, entitled "The World Trading System and Culture: Looking at the Problem from a Cultural Perspective," Ivan Bernier offered a further elaboration of what an international instrument on cultural diversity might contain. He noted that attempts to resolve the tension between trade and culture have been limited to subtracting goods and services from the application of trade agreements by various means. These approaches have not succeeded because they do not deal with the broader problem of cultural diversity and because they look at the problem exclusively from a trade perspective. (3) On the other hand, Bernier feels the approach proposed by the

SAGIT could succeed because it would bridge cultural and trade concerns.

To understand more concretely how the instrument would operate, he feels it is necessary to look at the principles that underlie the concept of cultural diversity, principles already expressed in a number of international agreements, resolutions and declarations. (4) Briefly stated, in order of importance these four principles are that:

1) culture is of crucial importance as a means of individual and social communication and development;
2) cultural patrimony is a crucial component of the identity and self-understanding of a people and for that reason must be protected;
3) authors have a right to the protection of their moral and material interest as regards their creations; and
4) cultural exchanges are fundamental for the promotion of understanding between peoples and for the dissemination of culture for the well-being of humanity and the progress of civilization. (4-7)

Bernier notes that a comparison of the cultural approach above with the trade approach, as instruments of development, reveals a reversal in the order of priorities. He sees this difference in perspective as at the heart of the culture/trade debate. (8) He briefly discusses the difficulty of deciding with which international organization to house the instrument – UNESCO or the WTO – and whether it would be better not to house it with any organization at all. (9) Bernier also points to the need to develop a consensus on this issue at the international level, a process in which he feels the International Network on Cultural Policy will play a crucial role. (9)

Following the release of the SAGIT report, in the 1999 Speech from the Throne, the Government of Canada announced its intention to develop a new approach internationally to support the diversity of cultural expression. In its Response to the Report of the Standing Committee on Foreign Affairs and International Trade, *Canada and the Future of the WTO,* June 1999, the government indicated that it will try to build support for this strategy with domestic stakeholders and in such forums as the International Network on Cultural Policy, UNESCO, the WTO, the OECD and La Francophonie and, pending developments with respect to the negotiation of a new agreement, will continue to seek the maximum flexibility in international agreements to pursue its cultural policy objectives.

Concluding Remarks

As the preceding literature review indicates, although opinion on the subject of trade and culture is divided, certain key messages can be clearly delineated. Trade is not an end in itself, but the means to a broader objective – a better society. The significance of cultural works is also social and political as well as economic. The pursuit of national cultural objectives is just as important as foreign and trade policy objectives. Cultural goods and services are *not* like other forms of merchandise. Cultural diversity is preferable to homogeneity. Governments have an important role to play in promoting and preserving cultural diversity.

Although economic integration is a global phenomenon, having an impact on cultures around the world, in the Canadian context the debate is really about Canada and the impact on Canada of our largest trading partner and closest neighbour, the United States. Given this geographical proximity, a common language shared by the majority of their citizens, common historical roots, and common influences on legal and political traditions and economic development, it is not surprising that the influence of American culture on Canadian culture, particularly English-Canadian culture, is overwhelming. A number of different theoretical models underlying cultural development policy and programs have been outlined in the articles reviewed. Many authors perceive the efforts of the United States in forcing the model they favour, the market-driven model, on other nations through trade agreements as a threat to global cultural diversity.

At the heart of the debate are the cultural industries, which act both as instruments for the communication of Canadian culture and as the bond that holds Canadians together – not just in the narrow sense of the arts, but in the larger meaning of our pastimes, habits, images, institutions, perspectives on the world and collective memory. Since the coming into force of the Free Trade Agreement in 1989, the effectiveness of the cultural exemption has been the focus of a great deal of discussion. Although views differ considerably, there appears to be a consensus that the exemption is not working. A number of different alternatives have been outlined in the literature, but nearly all are based on a common premise: a rules-based system is preferable to one where the uncertainty created by continued legal challenges and retaliation is weakening, bit by bit, the viability of Canadian cultural policy.

There also seems to be a growing opinion that content and investment rules aimed at ensuring space for "Canadian voices telling Canadian stories" are not accomplishing their intended objectives. A number of commentators have suggested how this might be remedied, with general agreement among them that more emphasis needs to be placed on ensuring truly "Canadian" content. Some authors have also described how technological changes occurring in Canada's cultural industries are hastening the development of new media, namely interactive video, audio and text-based services rooted in the convergence of telecommunications, computing and broadcasting. These changes are challenging traditional economic and regulatory models for the cultural industries and underline the need to rethink them.

For any new approach to succeed, it will also be important for those nations that sign on to clearly accept the basic principles that underlie it. Getting agreement on these principles, particularly from our largest trading partner, will be one of our greatest challenges. In this context, as several authors have indicated, it is important to understand that the position of the United States is also founded on basic principles and a history of government support for cultural endeavours. It will also be important to continue to strengthen the emerging international consensus on the need for a cultural diversity instrument.

Trade liberalization has a direct economic impact on Canada's cultural industries and by extension on Canadian culture, but what impact does the consumption of massive amounts of foreign cultural products and services have on Canadian identity? Current research cannot answer this question definitively. Research does indicate that Canadians have cultural values and attitudes that are different from those of Americans, but it also indicates that these differences are growing less and less as they converge toward a common set of North American values. This is not Americanization, but part of a hemispherical and global phenomenon. Values and attitudes change very slowly, over generations. Although free trade has probably acted as a catalyst in this process, it is clearly not the only catalyst for change. What is unclear is where, ultimately, this convergence of values will lead us, and whether, at the end of the day, it will determine our ability to remain distinctly Canadian. It is still too early to tell.

Finally, a growing number of observers in Canada and abroad are expressing concern that the integration of economies around the world is leading to increasing pressures being placed on the "social contracts" that hold our societies together. There seems to be little doubt that economic integration is having an impact on social cohesion; however, this does not have to represent economic determinism. The nation-state is not irrelevant. It still has an important role to play in ensuring that the negative impacts of economic integration are mitigated and that its benefits are shared by all members of society.

A number of the researchers whose works have been reviewed in this paper have identified gaps in our knowledge of the relationship between economic integration and culture. In this context, it is worth noting that as part of the Trends Project a number of research teams are currently undertaking research of direct relevance to trade liberalization and culture, identity and social cohesion. Their research will address such questions as: What effect does globalization have on the shaping of identity? On social systems? On the common institutions within which people live and work? On the maintenance and development of social cohesion? What is different about North American integration today, and what does this mean for things Canadians care about? What is likely to happen to North American integration in the next decade? What can be done to preserve and enhance the opportunities and minimize the risks from North American integration? The results of this research are expected to be available sometime in the year 2000.

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International Trade, Health Systems and Services: A Health Policy Perspective

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Introduction

International trade in health services is neither new nor entirely unfamiliar. For example, Canada trades in health services every time a Canadian "snowbird" obtains medical care in Florida. There is international trade whenever local nurses or doctors go abroad to work, or foreign practitioners come to Canada. Health services are traded when doctors and hospitals hook up across international borders via telecommunications systems to collaborate on the delivery of health services. And trade takes place when a Canadian health services company operates abroad, or a foreign-owned company delivers services here.

Relatively new, though, are international trade agreements that establish legal frameworks of binding rules for trade in services, including health services. This is nowhere more evident than in the World Trade Organization (WTO) and its General Agreement on Trade in Services (GATS). In 1994, more than a hundred WTO members completed the Uruguay Round of trade negotiations that included the GATS.

According to the WTO Secretariat, "the Uruguay Round agreement on trade in services is perhaps the most important single development in the multilateral trading system since the GATT[1] itself came into effect in 1948."[2] The Secretariat further explained that the GATS "extends to all forms of international trade in services" and "...because such a large share of trade in services takes place *inside* national economies, that its requirements will from the beginning necessarily influence national domestic laws and regulations in a way that has been true of the GATT only in recent years."

All services, including health services, are covered by the GATS services classification. GATS provisions require WTO members to progressively liberalize trade in services over time. In other words, there will be successive rounds of negotiations, beginning in 2000, to reduce or eliminate trade barriers and discriminatory trading practices worldwide.[3]

This paper explores some of the links between international trade and health services from a health policy point of view. Trade in health services can have far-reaching consequences for the health sector and health, and can create conflict between trade/economic goals and health/social objectives. It is, therefore, important for the health policy and research communities, as well as the trade policy community, to identify and address the key issues raised by trade in health services.

The potential dollar value of international trade in health services is enormous. The paper begins, therefore, with a brief look at the extent of health spending globally and in industrialized countries. An examination of the role of the public and private health sectors, particularly in the financing of health care, but also in the delivery of these services, makes clear that this sector is not just another form of commercial activity. A framework is suggested for considering the interrelationships between international trade and health. The core issue is the significance of international trade for achieving health objectives. How trade impacts on health involves both trade in goods (health and non-health goods) and trade in services. But the relationship goes much further. International trade can influence key determinants of health as well.

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[1] General Agreement on Tariffs and Trade; this covers trade in goods (e.g. health goods would include medical devices and equipment, pharmaceuticals).

[2] World Trade Organization Secretariat, *Guide to the Uruguay Round Agreements* (The Hague: Kluwer Law International, 1999), 161.

[3] Note: the launch of negotiations on services in 2000 was mandated in the Uruguay Round agreement itself, as part of the "built-in agenda," and was not dependent on a new round getting underway.

A more detailed examination of international trade in health services occupies the rest of the paper. According to the GATS, trade in services takes place in four modes: when services cross borders, when consumers go abroad, or by the mobility of capital and labour. These modes of trade in services are looked at in terms of their possible meaning for health services; the broader implications for health systems and health objectives are also considered.

The Health Sector

Spending on health

The sheer size of global annual expenditures on health care goods and services – about US$3 trillion[4] – is suggestive of the potential economic impact of trade liberalization. To put this in some context, world trade in all goods and services was US$6.7 trillion in 1998. Trade in services was US$1.3 trillion, or about 20 percent of that total.[5] In the United States, the world's leading exporter, health services are among the top 10 services exports (health services exports totalled US$921 million in 1997.[6]

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[4] G. Wolvaardt, "Opportunities and Challenges for Developing Countries in the Health Sector," in S. Zarrilli and C. Kinnon (eds.), *International Trade in Health Services: A Development Perspective* (Geneva: United Nations, WHO, 1998), 63-70.

According to the Organization for Economic Co-operation and Development (OECD),[7] health care services are one of the largest industries in its member countries. Although health expenditures as a percentage of gross domestic product have stabilized in recent years, OECD countries spent, on average, 8.1 percent of GDP on health in 1997. The GDP share was highest for the U.S. at 13.9 percent, and lowest for Turkey at 4.9 percent. Canada spent 9.2 percent of GDP on health, while the European Union and Japan spent 8.0 percent and 7.2 percent respectively.

Payers and providers

The public sector is, by far, the largest financier of health services among OECD countries. From 1970 to 1990, public sector health spending within the OECD grew to 74.2 percent of total health spending as governments undertook to make health services more accessible to their populations. There was then a period of decline in the public sector share of health spending as governments tackled continuously escalating health costs. By 1997, OECD member governments were financing, on average,

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[5] World Trade Organization, "WTO Services and Agriculture Negotiations: Meetings Set for February and March" (Press Release, February 7, 2000).

[6] U.S. Department of Commerce, International Trade Administration, "Top Ten Services Exports, 1997" (http://www.ita.doc.gov/sif/topten.htm).

[7] OECD, Employment, Labour and Social Affairs Committee, Working Party on Social Policy, *Trends in Health Expenditure 1970-1997* (DEELSA/ELSA/WP1(99)17, September 30, 1999).

73.7 percent of total health spending in their countries. In the European Union, 76.6 percent of all health spending was publicly financed, while the U.S. and Korea with a public share of 46.4 percent and 45.5 percent respectively were clear outliers among OECD countries.[8]

In Canada, total health expenditures (goods and services) for 1999 were approximately $86 billion.[9] This represents 9.2 percent of Canada's GDP, a share that has been relatively stable since 1995, even though the annual rate of growth in total health expenditures has accelerated (from an annual rate of growth of 1.4 percent in 1995 to 5.1 percent in 1999). The public sector remains the predominant source of health financing in Canada, accounting for approximately 70 percent of all health spending in 1999, although this is down from approximately 75 percent in 1991. Health spending is a major component of provincial governments' budgets, being roughly one quarter to a third or more of total budgetary spending depending upon the province.

According to the Canadian Institute for Health Information, private health spending in Canada consists mainly of out-of-pocket outlays by households and spending by private health insurance firms for supplementary or additional health benefits not covered or only partially covered by governments (e.g. primarily dental and drug services, but also the services of various health providers).

In 1999, about 62 percent of Canada's total health spending was accounted for by three categories: hospital services (32.5 percent), drugs (15.2 percent) and physician services (13.9 percent). Given Canada's universal, publicly financed system for necessary hospital and physician services, it is not surprising that almost 92 percent of total spending on hospital services and 99 percent of all spending on physician services are paid for publicly. Public health services (e.g. public health nursing and health promotion) are 100 percent publicly financed, and 57 percent of health research is financed publicly.

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[8] The U.S., other than for its Medicaid and Medicare programs for the poor and elderly, relies primarily upon private sector financing and market forces in its health system.

[9] Based on a forecast by the Canadian Institute for Health Information, *National Health Expenditure Trends: 1975-1999* (Ottawa: 1999).

Private financing is the dominant source of funds for dental services (94 percent); vision care (90 percent); prescription drugs (59 percent); non-prescribed drugs (100 percent); and services of other health professionals such as chiropractors, physiotherapists, psychologists, private duty nurses and naturopaths (69 percent).

Public financing does not necessarily mean public delivery of health services. Among OECD countries, most health systems fall into one of the following categories:[10]

- mainly private providers with a mix of public and private financing;
- mixed public and private providers with mainly public financing; or
- mainly public providers and mainly public financing.

Canada's health care system is generally described as being largely publicly financed and privately delivered. This, however, oversimplifies the relationship between public and private health sectors in financing and delivering health services. The accompanying table, adapted from the National Forum on Health's examination of Canada's health system in the mid-1990s, illustrates more fully the interface between the two sectors.[11]

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[10] OECD, *The Reform of Health Care: A Comparative Analysis of Seven OECD Countries,* Health Policy Studies No. 2 (Paris: OECD, 1992), 13.

[11] National Forum on Health, *The Public and Private Financing of Canada's Health System* (Ottawa: 1995).

Table 1: Financing and Delivery of Canada's Health Services

Service type	Financing	Delivery
Hospital services	100 percent public for medically necessary services; private for non-medically required hospital services or upgraded accommodation	Mixed public/private. Varies by province. Generally strong government regulation of sector
Physician services	100 percent public for medically necessary services (no extra billing allowed); private payment for non-medically necessary services	Private physicians are independent and self-regulating: some models of primary care delivery are more akin to government agencies (e.g. CLSCs in Quebec)
Services in private clinics	Privately funded if service is not medically necessary; some clinics charge patients a facility fee for medically necessary services over and above the funding provided by the provincial health insurance plan	Privately owned and operated – limited regulation
Dental/ optometry care	Mostly private (insurance or out-of-pocket); some provincial plans provide coverage for children and seniors	Private and self-regulating – i.e. dentists and optometrists
Prescription drugs	Mixed public/private; provincial plans pay for approximately 40 percent of all prescription drugs dispensed outside hospitals. Coverage is typically limited to seniors and welfare recipients. Drugs dispensed in hospitals are covered in hospital budgets. Balance is funded by a combination of private insurance plans and out-of-pocket	Private – delivery includes prescription by physician and dispensing by pharmacist or hospital

Non-prescription drugs	Mostly private (out-of-pocket)	Private – over-the-counter
Services of other professionals	Mostly private (insurance or out-of-pocket) – with limited coverage by provincial plans	Private (e.g. psychologists, physiotherapists, chiropractors, midwives, private duty nurses)
Alternative medicines	Mostly private (insurance or out-of-pocket)	Private – e.g. naturopaths, homeopaths, practitioners of oriental medicine, traditional Aboriginal healers
Long-term care (residential)	Mixed public/private; public portion covers insured health care services; private portion covers room and board	Mixed public/private
Home care	Partial public coverage provided in most jurisdictions; informal caregivers play an important role	Mixed public/private
Ambulance services	Partial public coverage in some provinces; special programs for residents of remote areas	Mostly private operators
Public health programs	Public	Public
Services to status Indians and Inuit	Public	Mixed public/private (federal government employees deliver some services directly)

The nature of health care: public good or private commodity?

Commercial trade in health services has enormous economic potential. Yet actual trade volumes are relatively low, liberalization is little in evidence, and governments remain significant players in the sector. Why that is the case needs to be investigated and understood.

For Drache and Sullivan,[12] the defining or core issue concerning public and private health is whether health care is a commodity or public good. Is it a public good that states should provide, or a commodity like any other that should be subject to market rules and disciplines – and, one would add, subject to trade and its liberalization?

There is overwhelming evidence that health care is *not* a normal market commodity; and health care markets are *not* ideal.[13] [14] [15] [16] [17] No major developed country treats health care like just another market commodity, or distributes it through normal market mechanisms.[18] [19] Chief among the reasons are:

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[12] D. Drache and T. Sullivan (eds.), "Health Reform and Market Talk: Rhetoric and Reality," in *Market Limits in Health Reform: Public Success, Private Failure* (London: Routledge, 1999), 1-21, p. 5.

[13] J. White, *Competing Solutions: American Health Care Proposals and International Experience* (Washington, D.C.: The Brookings Institution, 1995).

[14] OECD, *The Reform of Health Care: A Comparative Analysis of Seven OECD Countries,* op. cit.

[15] OECD, *Health Care Reform: The Will to Change*. Health Policy Studies No. 8 (Paris: OECD, 1996).

[16] World Trade Organization, Council for Trade in Services, "Health and Social Services: Background Note by the Secretariat," S/C/W/50 (Geneva: World Trade Organization, September 18, 1998).

[17] National Forum on Health, *The Public and Private Financing of Canada's Health System,* op. cit.

[18] Ibid.

[19] J. White, *Competing Solutions: American Health Care Proposals and International Experience,* op. cit.

- the fact that health care is based on needs, not wants; and access to care should not be based on ability to pay;
- the unpredictability of need for health care and the relatively high burden of payment in the absence of insurance, as well as incentives for private insurers to avoid high-risk patients or limit insured coverage for costly care; and
- the asymmetry of knowledge and information that favours care providers (physicians) and requires patients to rely upon their advice and approval for care.

The World Health Report 1999 has this to say on the issue:[20]

> Market mechanisms have enormous utility in many sectors and have underpinned rapid economic growth for over a century in Europe and elsewhere. But the very countries that have relied heavily on market mechanisms to achieve the high incomes they enjoy today are the same countries that rely most heavily on governments to finance their health services. Therein lies a lesson. Health is an important component of national welfare. Achieving high health outcomes requires a combination of universal entitlement and tight control over expenditure.

Evans[21] points to the fact that all industrialized countries but the United States have opted for universal public payment systems to provide their principal health services. Broadly speaking, these systems share such features as more or less universal insured coverage, comprehensive coverage of principal benefits, income-based contributions, administrative mechanisms to control costs, and a primary role for the state in financing and/or regulating for purposes related to, for example, cost control or equity of access.

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[20] World Health Organization, *The World Health Report 1999: Making a Difference* (Geneva, 1999), 33.

[21] R. Evans, "Health Reform: What Business Is It of Business?" in D. Drache and T. Sullivan (eds.), *Market Limits in Health Reform: Public Success, Private Failure* (London: Routledge, 1999), 25-47.

Not even the widespread reform of European health systems over the 1980s and 1990s to seek greater efficiency, effectiveness and patient choice and influence altered the primary role of the state in ensuring access to health services. In their analysis of these reforms, Saltman and Figueras[22] conclude that western European countries maintained their commitment to universal access and sustainable financing and did not shift from publicly to privately accountable funding.

Tuohy[23] observes that even in the climate of fiscal pressures in the last two decades, publicly financed health systems in OECD countries did not reduce eligibility for insured coverage as a possible response to these pressures. In fact, during this period, two countries, the United States and the Netherlands, attempted to increase the role of the state in health care and expand publicly insured coverage for their citizens. Neither initiative succeeded, a fact Tuohy ascribes to the difficulty of expanding public programs in the fiscal climate of the 1990s.

International Trade in a Health Policy Framework

In a health policy framework, the core international trade issue concerns the consequences of trade for achieving health objectives, such as those set out for health systems by the World Health Organization:[24]

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[22] R.B. Saltman and J. Figueras, "Analyzing the Evidence on European Health Care Reforms," *Health Affairs* (March/April 1998): 85-108.

[23] C.H. Tuohy, *Accidental Logics: The Dynamics of Change in the Health Care Arena in the United States, Britain and Canada* (New York: Oxford University Press, 1999).

[24] World Health Organization, *The World Health Report 1999: Making a Difference*, op. cit., 32-33.

- improving health status;
- reducing health inequalities;
- enhancing responsiveness to legitimate expectations;
- increasing efficiency;
- protecting individuals, families and communities from financial loss; and
- enhancing fairness in the financing and delivery of health care.

There are a number of ways that international trade can impact on health systems and health objectives.[25] Trade in goods is one way. Such trade may be in health goods (e.g. pharmaceuticals, medical devices, equipment) that consumers buy directly or that health systems use in the provision of care, or it may be in the form of non-health goods (e.g. hazardous wastes and materials, unsafe industrial technologies,[26] tobacco) that can affect health.

Pharmaceuticals provide an example. Some trade agreements provide for international enforcement of patent protection. This is the case in both the North American Free Trade Agreement (NAFTA) and the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). While the importance and benefits of intellectual property protection in terms of stimulating innovation are widely recognized, patent protection provisions are raising issues concerning the production of needed drugs, drug prices, access to necessary medications and health system costs.[27] [28]

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[25] D.W. Bettcher, D. Yach and G. E. Guindon, "Global Trade and Health: Key Linkages and Future Challenges," *Bulletin of the World Health Organization* (2000), 78 (4): 521-534.

[26] D.B. Menkes, "Exporting Hazards to Developing Countries," *World Health Forum* (Vol. 19, 1998): 412-416.

[27] C.M. Kinnon, "World Trade: Bringing Health into the Picture," *World Health Forum* (Vol. 19, 1998): 397-405.

Access to medicines in developing countries is one concern. For example, in response to criticism of U.S. trade policy to enforce drug patents of U.S. pharmaceutical companies, President Clinton announced a new policy at the 1999 Seattle WTO Ministerial meeting to ensure access to medicines for the world's poorest people. The United States Trade Representative and Health and Human Services have implemented a co-operative approach on health-related intellectual property issues to address cases where U.S. trade law related to intellectual property significantly impedes a foreign government's ability to deal with a health crisis.[29] This resulted in an Executive Order of May 10, 2000, to allow sub-Saharan African countries to provide residents with better access to HIV/AIDS drugs and medical technologies to combat AIDS.[30]

Food products and their safety are another example. Sanitary and phytosanitary measures in trade agreements are there to, among other things, protect human health from unsafe food. No one doubts the importance of ensuring the safety of food in the global trade environment. There is, however, a growing issue of whether the WTO's Agreement on Sanitary and Phytosanitary Measures favours commercial trade over health interests. High-profile and controversial WTO dispute challenges concerning growth hormones in beef and British beef (the "mad cow disease" issue) have fuelled debate over trade protectionism, the precautionary principle and how countries assess and manage risks to protect health in the international trading system.

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[28] "Sleep Less in Seattle," *The Lancet* (Vol. 354, December 4, 1999): 1917.

[29] USTR, "USTR Releases Super 301, Special 301 and Title VII Reports" (Press Release, May 1, 2000).

[30] The White House, "Executive Order: Access to HIV/AIDS Pharmaceuticals and Medical Technologies" (Press Release, May 10, 2000).

A second major way that international trade can impact on health is through trade in health services. This trade may be in services directly related to the provision of health services, such as trade in hospital, physician and nursing services, or it may be trade in affiliated services in the health sector, such as health insurance, health facility management, or educational services in the health field. It is the links between this kind of trade and health that this paper will focus on in the next section.

A third way that trade can impact on health is through the relationship between trade, the economic outcomes it may produce (e.g. growth and development, productivity gains, improved prosperity, higher standards of living, and job creation) and the broader determinants of health. To the extent that international trade improves such outcomes, there is the possibility, according to a determinants-of-health approach, for population health to benefit.[31] For instance, trade that creates jobs has the potential to improve health because of a positive relationship between employment and health.

But, by itself, trade's impact on broader health determinants is no guarantee that desirable health outcomes will follow. Sound health policies on access and equity to health services are a necessary condition. For example, Amartya Sen,[32] the Nobel Prize winning economist, reminds readers that it would be a mistake to take as the main lesson that economic prosperity is related to good health. The link is there: economic prosperity and good health are positively related. But the relationship is more complex. The "finer points" of the relationship, as Sen notes, suggest that good health, in the form of longevity, is more likely to materialize when economic prosperity works through poverty removal and public health care. For Sen, it is how the fruits of economic growth are used – particularly in the form of a commitment to public health care – that matters most for better health outcomes.

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[31] R. Evans, M. Barer and T. Marmor, *Why Are Some People Healthy and Others Not?* (New York: Aldine de Gruyer, 1994).

[32] A. Sen, "Economics and Health," *The Lancet* (Vol. 354, December 1999): siv. 20.

A similar, broader point was made in the *Human Development Report 1999* regarding the relationship between trade, growth and human development.[33] In looking at countries such as Egypt, Pakistan, Russia, the Republic of Korea, Botswana, Chile, Malaysia and Thailand, the report concluded that a strong link between trade and growth is no guarantee of a strong link with human development and well-being. Trade and growth need to be accompanied by a comprehensive package that, depending upon the country situation, includes economic, social and governance reforms, in order to improve welfare.

International Trade in Health Services and the GATS

With the GATS of 1994, a multilateral discipline with basic rules for liberalizing trade in all services was established. As a legal framework, the GATS aims to reduce or eliminate measures that prevent or discriminate against the provision of services across borders, or against foreign-owned services or foreign service providers in the market of another economy. This agreement has been called a "landmark" for creating multilateral disciplines in the "virgin" territory of services and, up to now, a "failure" in establishing freer trade in services.[34] Proponents of trade liberalization are counting on this changing when WTO members negotiate "progressive liberalization" of services as required in the agreement. A new round of GATS negotiations, begun in February 2000, will test how far WTO members are prepared to liberalize trade in services in general, and trade in health services in particular.

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[33] United Nations Development Programme, *Human Development Report 1999* (New York: Oxford University Press, 1999).

[34] B. Hoekman, "Assessing the General Agreement on Trade in Services," in W. Martin and L.A. Winters (eds.), *The Uruguay Round and the Developing Countries* (New York: Cambridge University Press, 1995), 327-364.

GATS covers all services except those "supplied in the exercise of governmental authority," which it defines as services that are neither delivered on a commercial basis nor in competition with other service suppliers (GATS Article I (3)(b)(c)). The WTO Council for Trade in Services appears to suggest that this Article would apply only in the case of a rather pure form of governmental supply of health services – that is, direct, free-of-charge government provision of medical and hospital treatment without private sector involvement.[35] Despite the Council's attempt at clarity, the meaning of this Article and its application to publicly financed health services with mixed public/private delivery is far from clear. An examination of this element in the GATS, however, is beyond the intent of this paper. Clearly though, this "exemption" has major significance for the health sector and WTO members' strategic approaches in current and future GATS negotiations.

Under the GATS, services are delivered through one or more of the following modes:

- mode 1: cross-border – the service, not the supplier, crosses national borders;
- mode 2: consumption abroad – the consumer crosses national borders to receive a service;
- mode 3: commercial presence in the consuming country – a foreign-owned facility supplies the service in the territory of another country; and
- mode 4: temporary movement of natural persons – foreign service suppliers cross national borders to provide the service.

Trade liberalization of services entails specific GATS commitments being made by a WTO member, in one or more of these modes of supplying services, to allow access to its domestic market (market access), and/or to treat foreign companies and/or providers on the same footing as domestic companies/providers (national treatment). There is a general obligation in the GATS for WTO members to accord most favoured nation treatment (MFN) to all other WTO members unless a specific exemption on MFN has been taken.

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[35] WTO Council for Trade in Services, "Health and Social Services: Background Note by the Secretariat," op. cit.

How do the GATS modes of service delivery apply to health services? What are possible implications, in terms of potential opportunities and costs, if health services are liberalized in these modes? What are some typical barriers to trade in the four modes of services? On what modes of service supply have countries liberalized their trade in health services? These and other questions are explored in the next sections.

Mode 1: cross-border trade in health services

In this GATS mode of service supply, the service itself moves across national borders (movement of services). Telehealth and telemedicine[36] are the most cited examples of cross-border services trade in the health field. These technology- and knowledge-based health services are playing a larger role in the health field as governments worldwide search for solutions to such issues as health care cost containment, access to needed health care, the quality of care, waiting lists, the supply and distribution of health human resources and public expectations of health care systems. An overview of some telehealth applications appears in Tables 2 and 3.[37]

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[36] As used by Industry Canada (Strategis website), the terms telehealth and telemedicine are defined as follows: telehealth: the use of information and communications technologies to deliver health and health care services and information over large and small distances; telemedicine: all forms of remote medicine – teleconsultations, telepathology, teleradiology, telepsychiatry, teledermatology, telecardiology, etc. In Europe, telehealth is called health care telematics.

Table 2: Telehealth Categories and Users

Category	Users
All forms of medicine-at-a-distance: teleconsultations, telepathology, teleradiology, telepsychiatry, teledermatology, telecardiology, etc.	Physicians, health care professionals, health care institutions
Inter-institutional, patient and clinical records and information systems, electronic health and clinical records and databases accessible by network	Health care institutions, professionals and workers, physicians' offices, researchers
Public Health and Community Health Information Networks (CHINs) and multiple-use health information networks	Government (including policy makers), epidemiologists, public health professionals, physicians' offices, pharmacies, clinics and CHINs
Tele-education and multimedia applications for health professionals and patients, and networked research databases; Internet services	Universities and colleges, associations, researchers, physicians, health care professionals, patients
Telemonitoring, telecare networks, telephone triage, remote home care, and emergency networks	Consumers, elderly, chronically ill, disaster and accident victims, telenurses, call centre users or operators

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[37] Industry Canada Strategis website, "Sector Competitiveness Framework Series: Telehealth Industry, Key Points about This Industry" (1998).

Table 3: Telehealth Applications that Can Facilitate Health Care Procedures

Health care procedures, process	Possible telehealth application
Telephone-based or face-to-face consultation between specialists and general practitioners	Videoconferencing, IATV, computer-based e-mail
Physical transfer of medical images for specialist opinion on radiographs, ultrasound, computed tomography scans, pathology slides	Electronic transfer of images to specialists; comparison of images against banks of stored electronic slides and images for comparison
Handwritten, paper-based patient files and charts	Palm-top pen-based computer tablets, desktop workstations, computerized patient records
Handwritten, paper-based prescriptions	Electronic prescription ordering using a CHIN, HIN or pharmanet
Consulting Compendium of Pharmaceuticals and Specialties, 32nd ed. (Ottawa: Canadian Pharmacists Association, 1977) for information on drug being prescribed	Drug interaction software, drug information database online
Home visits unassisted by technology	Laptop or portable computer with modem to communicate with physician or health care institution
Home care, elder care	Telemonitoring from the home, assisted devices and technologies
Visits to the emergency room of the local hospital	Telecare, teleassisted triage, 1-900 telephone calls to obtain assistance, video visits
Referrals from general practitioner	Appointments by e-mail, electronic scheduling by general practitioners
Patient travelling from remote location if requiring specialized counselling, diagnosis or treatment	Video-consultation with specialist from afar
Literature search in medical library for current literature on new	Electronic search from home or office using Medline or other

procedures, clinical trials, etc.	medical information management and database retrieval service
Travel to another location for grand rounds, continuing medical education, conferences, meetings, seminars	Attendance from home or office via audio, video or computer conferencing, or interactive TV
Clinical trials	Clinical trial management systems, expert advice online

Expectations are that the worldwide growth in telehealth/telemedicine services will be considerable. For example, the potential demand for several such services in 2000 was projected to be as follows:[38] [39]

- telemedicine services in their various forms at about US$1.1 billion;
- direct patient care telehealth services at about US$800 billion;
- continuing professional education at about US$3.9 billion; and
- online health information, which now occupies about 10 percent of total Internet content, at about US$21 billion.

The implementation and use of telehealth/telemedicine services, even *within* national health systems, raise such issues as the recognition of credentials and licensure; legal liability and malpractice considerations, including provider insurance coverage; provider remuneration; patient privacy and confidentiality; the existence of enabling infrastructure and compatibility of standards in such areas as data, images and medical records; infrastructure and future operating costs; the extent of demand for such care and the cost implications; and the quality and appropriateness of care.

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[38] Feedback Research Services, January 1996, quoted in Industry Canada Strategis website, Ibid., p. 100.

[39] Industry Canada, "Life Sciences Branch – Health Industries: Canadian International Business Strategy (CIBS) 1999-2000: Health Services, 2000," Strategis website (http://strategis.ic.gc.ca/SSG/ht01195e.html).

Some indication of Canadians' changing relationship with the health system, particularly as it concerns health information, comes from a recent survey that found the Internet to be the principal information source on health for 8 percent of Canadians.[40] This figure jumps to almost 28 percent for those without a family physician. Of those relying on the Internet for health information, one third did so for self-diagnosis, while one third used it to check a diagnosis from their doctor. A majority of respondents favoured being able to ask doctors questions electronically, making appointments online and being referred to specialists via e-mail. Using the Internet for drug prescription refills was supported by about 40 percent, while 33 percent thought online annual check-ups were a good idea.

In his look at the Internet in the United States, Goldsmith makes the point that use of this new technology has the potential to significantly change the interaction between consumers and the health system.[41] Using the Internet for health information is a prime reason why people log on: 70 million Americans sought health information on the Internet in 1999. He points out that it is not unusual now for individuals to access health and medical information and data that previously were only available to health and medical providers. Goldsmith regards the resistance of the medical profession to adopting Internet technology, and privacy and confidentiality issues as the two major hurdles facing the spread of the Internet's use for health services.

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[40] A. Picard, "Media Main Source of Medical Data: Poll, Health Information Comes from All Sources," *The Globe and Mail* (July 5, 2000).

[41] J. Goldsmith, "How Will the Internet Change Our Health System?" *Health Affairs* (January/February 2000, Vol. 19, No. 1): 148-156.

In the United States, a concern with protecting consumers against illegally dispensed drugs may lead to new laws to regulate the sale of prescription drugs over the Internet. More than 200 websites are being investigated for possibly selling unapproved drugs or approved medications without valid prescriptions.[42]

A recent U.S. study on the privacy policies of 21 health information websites found that these sites held unprecedented amounts of personal health information supplied by site visitors. The problem, however, is that the personal health information is shared without the knowledge or consent of the person who provided this information – information available to third-party networks allowed them to construct detailed, personally identified profiles of individuals' state of health. According to the study's authors, the privacy policies of the various websites fell short of giving adequate privacy and confidentiality protection.[43]

In the United States, a report by the National Research Council on Internet use in health care cited the need for new policies to regulate the protection of electronic records containing health information and to address the reimbursement of doctors. The report also noted that state licensure practices are currently a barrier to interstate provision of telemedicine services.[44]

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[42] Bureau of National Affairs, "FDA Warns Foreign Online Drug Sites that Sales to United States May Be Illegal," *Health Care Policy Report* (Vol. 8, No. 6, Feb. 7, 2000): 210.

[43] Bureau of National Affairs, "Health Information Web Sites Do Not Protect Consumer Privacy, Study Finds," *Health Care Policy Report* (Vol. 8, No. 6, Feb. 7, 2000): 234.

[44] Bureau of National Affairs, "Stimulating Internet Use in Health Care Requires New Technology, Policy, Report Says," *Health Care Policy Report* (Vol. 8, No. 9, Feb. 28, 2000): 342.

As well, a concern with the quality of Internet health care has led the Internet Healthcare Coalition to draft a code of ethics on business practices for Internet health care. The draft code will cover such areas as privacy, commerce, content and services, disclosure, and the practice of health care on the Internet. The Coalition also plans to conduct a global review of the draft code via online public hearings and consultations.[45] Finally, a U.S. survey of Internet sites of state medical boards used to post information about physicians disciplined by the boards found that most of the online information varied considerably, was difficult to access and inadequate to inform and protect consumers.[46]

International trade in telehealth and telemedicine services makes the complexity of issues such as these even greater, and their resolution more difficult. Some recent developments may be illustrative of the complications that can arise when health care services cross borders.

Canadian doctors who give advice or care to U.S. citizens via the Internet or telehealth may face significant risks if sued. The Canadian Medical Protective Association (CMPA) has informed doctors of its new policy not to cover and defend them in the case of a lawsuit in the United States arising from care provided to Americans in Canada.[47] The CMPA will continue to defend doctors in lawsuits by U.S. citizens in Canadian courts. One physician, commenting on this new CMPA policy, stated that issues around telehealth are "in flux" and still being debated

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[45] Bureau of National Affairs, "International Group Works Toward Ethics Code for Health Care Web Sites," *Health Care Policy Report* (Vol. 8, No. 6, Feb. 7, 2000): 231.

[46] Bureau of National Affairs, "State Medical Boards' Online Data on Disciplined Doctors Inadequate, Study Finds," *Health Care Policy Report* (Vol. 8, No. 6, Feb. 7, 2000): 235.

[47] J. Manzer, "Treating Americans: A Subsidy for Our Health Care?" *The Medical Post* (May 2, 200): 5.

(e.g. whether the treating doctor needs a licence in the patient's home location).

And the U.S. Food and Drug Administration has warned several foreign websites that their Internet sales of prescription drugs may be illegal. The possibility of an international strategy to combat illegal sales of pharmaceuticals also is being explored.[48]

Adams and Kinnon[49] of the World Health Organization Task Force on Health Economics assessed the possible implications for developing countries of trade liberalization in health services across the GATS modes of supply for three health objectives: equitable access to health services, quality of health services and efficiency of resource allocation. These authors concluded that, with so little trade in telemedicine currently taking place or known, there is no evidence one way or the other that health objectives will be advanced with trade liberalization. In this regard, the issue is not so much what such trade can or cannot do, but whether governments can harness it to improve equity of access, the quality of care or the efficiency of its delivery.

Mode 2: consumption abroad

In this form of service supply, it is the consumer who receives a service in another country by going abroad (movement of the consumer). Health services to tourists, and students going abroad for their health and medical education, are typically cited as examples in the health sector. The United Nations Conference on Trade and Development (UNCTAD) considers health services consumption abroad as the dominant mode of service supply – that is, most transactions in international trade in health services involve the movement of consumers for health care and education in the health/medical fields.[50]

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[48] Bureau of National Affairs, "FDA Warns Foreign Online Drug Sites that Sales to United States May Be Illegal," *Health Care Policy Report* (Vol. 8, No. 6, Feb. 7, 2000): 210.

[49] O. Adams and C. Kinnon, *Health Economics Technical Briefing Note: Measuring Trade Liberalization against Public Health Objectives: The Case of Health Services* (Geneva: World Health Organization, 1997).

Why UNCTAD, for example, counts health/medical education and training as part of the supply of a health service, rather than the supply of educational services, is not clear. The distinction between health services and educational services in the WTO services classification is clear. Health services are generally services intended to promote, maintain and restore physical, mental and social health and well-being. When students go abroad for health/medical education/training services, that is trade in educational services, not health services.

Another definitional issue concerns the circumstances under which the receipt of a health service abroad constitutes trade. Do all health services delivered to non-residents in another country qualify as trade? Are there criteria for determining when it is trade and when it is not trade? Is it, for example, a matter of who receives the services (i.e. non-residents and how that term is defined), who pays for the service (e.g. the patient, the patient's private health insurance, the patient's home country, the host country), or the health circumstances under which the service is delivered? Regarding the latter, one can distinguish two broad health circumstances: elective or non-emergency care and non-elective or care required on an urgent basis. A question then arises whether care delivered abroad to a non-resident (e.g. a tourist) on an urgent basis constitutes trade.

Very little is known about trade in health services, with neither data nor information readily available to answer questions such as the following: Other than under health emergencies, why do individuals seek health services abroad?

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[50] UNCTAD, *Preparing for Future Multilateral Trade Negotiations: Issues and Research Needs from a Development Perspective* (New York and Geneva: 1999).

What kind of health services do they seek and in what countries? Are they more or less likely to seek health services abroad if they have public versus private health insurance at home? How much of this care is paid for out-of-pocket versus by public health or private health insurance plans? What impact does the provision of health services to non-residents have on the health system of the supplier country, and on access and quality of care for residents of that country?

Among the reasons that individuals may seek care abroad are:[51]

- Such care is not available at home (e.g. care is sought in regions that offer special treatments or possess special facilities such as hot springs or spas).
- Such care is not insured at home.
- Care elsewhere is of higher quality or available from more prestigious facilities and providers, or of equal quality but lower cost.
- Obtaining care abroad is consequential to decisions to retire or spend part of the year in warmer climates.

A major barrier to the movement of consumers is the lack of portability of health coverage, either by public or private health insurers, across national borders. An exception would be private health insurance specifically for travellers to cover or help cover the costs of out-of-country emergency health care. For some developing countries, consumption abroad in the form of "health tourism" is seen as an important future source of trade, if a solution to the non-portability of benefits can be found.[52]

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[51] UNCTAD Secretariat, "International Trade in Health Services: Difficulties and Opportunities for Developing Countries," in S. Zarrilli and C. Kinnon, *International Trade in Health Services: A Development Perspective* (Geneva: United Nations, WHO, 1998), 3-34.

[52] D.D. Benavides, *Trade Policies, Export of Health Services in a Development Perspective*, Preliminary draft, Inter-regional Meeting on Health and Trade: Towards the Millennium Round, November 3-5, 1999, Washington, D.C.

According to the Industry, Trade and Technology Review in the United States, a global medical insurance plan was introduced in 1998 by the International Health Alliance that would allow one to travel anywhere in the world to receive medical care.[53]

In Canada, portability of insured coverage is one of five principles of the Canada Health Act (CHA), the federal health legislation governing federal government financial assistance to provincial governments' health care systems. The CHA's portability provisions include out-of-country portability for medically necessary hospital and physician services. This out-of-country portability is limited, however, to covering medically required services at payment rates in one's province of residence. Additionally, provincial health insurance plans can require prior approval for elective out-of-province care without contravening the Act. This latter feature allows health plans to control against individuals seeking care out-of-country when it is available at home, and serves as an important health system cost containment mechanism.

Rules governing the European Union also provide for the portability of medical benefits across member countries if the health care is required in an emergency.[54] Prior approval is needed for elective care in another EU country before the care will be paid for by the patient's home country. This condition governing elective care in another EU country, and its payment by the patient's home country, has been successfully challenged in court in what have become known as the Kohll and Decker cases. In both cases, the European Court of Justice ruled that reimbursement provisions were inconsistent with the EU's requirements for the free movement of goods and services, and that the rules of member states' social security systems had to comply with these free movement provisions.

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[53] D.R. Luther, "Health Care Services: Strong Fundamentals and Innovations Foreshadow Growth in U.S. Exports and Foreign Direct Investment," *Industry, Trade and Technology Review, Health Care Services* (June 1999): 19-25.

[54] V. Kendall, *The Prospects for Private Healthcare in Europe* (London: The Economist Intelligence Unit, June 1999).

These court rulings also may have broader implications for the extent to which EU members' social security systems, including health systems, remain the sole responsibility of member states, and outside the application of EU rules. For instance, in the Netherlands there is a concern that national law provisions requiring "solidarity contributions" by privately insured patients toward coverage for others under public health insurance may contravene EU rules on fair competition.[55] Similar concerns exist regarding the use of national and regional agreements on prices to control the cost and type of care, and certain rules set out in obligatory contracts between hospitals and insurers that may be seen as forming cartels and obstructing foreign competition.

In the absence of widespread portability of health benefits, one's financial capacity and willingness to pay for travel and treatment costs become determining factors in consumption abroad. In the United States, the treatment of foreign patients is the largest component of that country's exports in health services.[56] From 1992 to 1996, these exports grew at an average annual rate of 5 percent. The slower rate of growth of 2 percent in 1997 is attributed to currency devaluations that made travel and treatment costs more expensive for patients from Asia, Latin America and Canada.

A study by Anderson et al.[57] raises questions about the willingness of patients to pay more in order to obtain more timely access to care. A survey of patients in Manitoba, Canada; Barcelona, Spain; and Denmark on waiting lists for cataract surgery found limited support for paying higher taxes or out-of-pocket for more timely treatment in their home countries. What is interesting for trade considerations is: if patients *on waiting lists* are generally unwilling to pay more for faster treatment at home, how willing are patients in general to pay for care abroad, and what factors are significant in their decisions to seek such care?

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[55] T. Sheldon, "EU Law Makes Netherlands Reconsider Its Health System," *British Medical Journal* (Vol. 320, January 22, 2000): 206.

[56] D.R. Luther, "Health Care Services: Strong Fundamentals and Innovations Foreshadow Growth in U.S. Exports and Foreign Direct Investment," op. cit., 20.

[57] G. Anderson et al., "Willingness to Pay to Shorten Waiting Time for Cataract Surgery," *Health Affairs* (September/October, Vol. 16, No. 5, 1997): 181-190.

As noted earlier, currency fluctuations can deter foreign patients from seeking care in the United States. Can currency changes, along with lower relative treatment costs and quality health care, induce patients from the U.S. and elsewhere to seek care in Canada? An absence of data prevents systematic analysis of this question, but some examples are illustrative. A private facility in Toronto that performs hernia surgery reports that about 20 percent of its 7,000 annual operations are on American patients.[58] In British Columbia, a favourable Canadian exchange rate, lower treatment costs and good quality of care for laser eye surgery help to attract foreign patients, especially from the U.S. and Asia. One physician reports that 40 percent of his patients come from abroad; another notes that, in some months, more than half of his patients are from the United States.[59] One Canadian laser eye surgery clinic estimates that, each month, 40 percent to 50 percent of its clients at 15 clinics across Canada come from the United States.[60] This company has also expanded into the U.S. market partly in response to the possibility of fewer future American customers as the U.S. eye surgery business grows. Another laser eye surgery clinic, this one in British Columbia, advertises its services in Seattle and has a clientele that is about 90 percent American.[61]

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[58] C. Leslie, "The Private Clinic Debate," *The Medical Post* (May 9, 2000): 22-23.

[59] H. Kent, "Huge Declines in Price as Competition Heats Up in Vancouver's Booming Laser-Surgery Market," *Canadian Medical Association Journal* (Oct. 5, 1999), 161 (7): 857-858.

[60] L. Landon, "The Lure of the Laser: Cheap, Safe Eye Surgery Draws Americans to Canada," *The Ottawa Citizen* (July 11, 2000).

Another example, albeit for a health good rather than a service, is that of U.S. seniors, described in the media as "drug price refugees," busing to Canada to buy necessary medications at significantly lower cost.[62] The State of Vermont is examining the possibility of more formal arrangements with the Province of Quebec to facilitate access to medications from that province for Vermont residents. In a similar vein, U.S. Senate candidate and wife of U.S. President Clinton, Hillary Clinton, is reportedly proposing legislation to enable access for U.S. citizens to lower-cost prescription drugs sold in Canada.[63]

One of the barriers facing Canadian doctors when considering to treat American patients, and presumably patients from other countries as well, is the Canadian Medical Protective Association's policy of not defending doctors in lawsuits in American courts brought forward by American patients who have been treated in Canada.[64] Even precautions by a doctor to have U.S. patients sign a consent form/contract agreeing to the treatment and restricting any legal action to Canada and Canadian laws may not suffice to protect doctors if they advertised services to attract foreign patients. An expert in medical law, however, believes that doctors can protect themselves with service contracts that state clearly that the contract proceeds under Canadian law, and that any legal action and damages will be based on Canadian law. The same expert cautions doctors to ensure that their advertising to foreign patients is also clear on these matters.

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[61] C. Leslie, "The Private Clinic Debate," op. cit.

[62] I. Peritz, "U.S. Seniors Shopping in Canada for Drug Prescriptions Too Costly in States, Protester Says," *The Globe and Mail* (January 20, 2000).

[63] A. Nagourney, "Mrs. Clinton Favors American Access to Cheaper Canadian Medicines," *The New York Times* (February 9, 2000).

[64] J. Manzer, "Treating Americans: A Subsidy for Our Health Care?" op. cit. As noted earlier, this policy bears importantly on the decision to provide services through telemedicine.

What is known about Canada as an export source of patients for the U.S. health services market? In his article on U.S. health services exports, Luther[65] notes that there are no official data on exports of health services by country, but industry representatives he interviewed believe that Canada is the dominant export market, while other key markets include the United Kingdom, Germany, Mexico, Australia and Japan.

In one of the rare studies on Canadians' use of the U.S. health system, Katz, Verrilli and Barer found no support for the perception, popularized by critics of Canada's public health care system, that Canadians are frequent users of U.S. health services.[66] Data from Ontario's health insurance plan were analysed. It was found that Ontario spent US$1.1 billion on U.S. medical services between 1987 and 1995, but this represented less than 1 percent of the health insurance plan's total medical payments. Moreover, changes during the study period in Ontario's reimbursement policies for out-of-country health services resulted in dramatic declines in the amount of spending for these services from the levels that prevailed in 1987-1991, when the province's benefits were comparatively generous. There is evidence, according to the authors, that the United States is a destination for care when that care is not as readily available in Canada. An important shortcoming of the study, noted by the authors, is the omission of private health financing (i.e. spending for care in the United States via out-of-pocket payments and private health insurance).

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[65] D.R. Luther, "Health Care Services: Strong Fundamentals and Innovations Foreshadow Growth in U.S. Exports and Foreign Direct Investment," op. cit.

[66] S.J. Katz, D. Verrilli, M.L. Barer, "Canadians' Use of U.S. Medical Services," *Health Affairs* (January/February, 1998): 225-235.

The Canadian Institute for Health Information (CIHI) and Statistics Canada consider cross-border shopping by Canadians for health care to be too rare for reliable measurement in existing national surveys.[67] In the National Population Health Survey, 1998/99, fewer than 0.1 percent of respondents said they had been treated in the United States in the past year. CIHI data also show that 3,200 Americans were treated (mostly for hernia surgery) at acute care hospitals in several Canadian provinces.

At various times, some Canadian provinces have made temporary arrangements with nearby facilities in the United States to meet pressing health care needs beyond the capacity of local resources. For example:[68]

- At one time the British Columbia Cancer Agency sent patients to the United States for radiation treatment. The Agency is now considering sending 600 patients to U.S. facilities for such treatment.
- Ontario will spend $23.1 million for radiation treatment in the U.S. for 700 cancer patients.
- Quebec is sending several hundred cancer patients to U.S. facilities for treatment.

The need for such arrangements has been attributed to a shortage of radiation therapists, medical physicists and larger numbers of cancer patients in an ageing population.[69] Interestingly, even though this out-of-country care is paid for by the provincial health insurance plans, the same article reports that about half of patients referred abroad for treatment refuse to go abroad. Thus, the decision to seek care abroad is only partly explained by coverage and portability factors. Other factors of likely significance for the willingness to go abroad for care include the medical condition, urgency of treatment, duration of treatment, and proximity of treatment to home and family.

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[67] Canadian Institute for Health Information, Statistics Canada, *Health Care in Canada: A First Annual Report* (Ottawa, 2000), 13.

[68] "Guarding the Border: The U.S. Role in Canadian Care," *The Medical Post* (January 4, 2000): 1-2.

[69] L. Priest, "Want Health Care in Canada? Sign This Waiver," *The Globe and Mail* (January 8, 2000).

To summarize, while our understanding of individuals' decision making to seek care abroad is limited, the mix of factors goes beyond the portability of insured benefits and what trade negotiations can address. Economic considerations (e.g. ability to pay, currency fluctuations, the cost of care), personal factors (e.g. willingness to pay, willingness to go abroad), the nature of the health condition and need for care (e.g. elective vs. emergency care), and aspects related to the care itself (e.g. its quality, proximity of the treatment facility, duration of the treatment) and liability related to malpractice would all appear to play roles.

Finally and most importantly for health policy, a key issue is the implications that consumption abroad has for such objectives as equitable access to health care. As Adams and Kinnon[70] note, the major concern is that equity of access for local residents will suffer from a policy of exporting health services to foreign patients. In treating foreign patients, access to care becomes largely based on ability to pay for care, not one's need for care, which leads to preferred access for foreign, paying patients. There is a further concern about using or redirecting scarce financial, human and capital resources to serve the needs of foreign rather than local patients. The situation is more complex than this suggests, however, and an analysis of the risks needs to consider several aspects, including:

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[70] O. Adams and C. Kinnon, *Health Economics Technical Briefing Note: Measuring Trade Liberalization against Public Health Objectives: The Case of Health Services*, op. cit.

- the mode of financing of the health system – public or private;
- the extent of insured coverage by the health system – universal or selective;
- the particular health services being promoted for consumption abroad, taking into account how these are financed by the health system and whether they fall inside or outside the basket of insured services;
- the capacity of the health system to provide care to foreign patients – whether there is excess capacity or the system is already stretched to its limits;
- the health needs of the population versus those of foreign patients (e.g. basic health needs vs. highly specialized needs);
- whether the facilities and providers treating foreign patients are inside or outside a publicly or privately financed health system; and
- whether the revenues generated from treating foreign patients go to the public or private sector, and what use is made of these revenues (e.g. whether they go to improve the health system or other determinants of health such as education or employment).

Mode 3: commercial presence

In mode 3, services are supplied by a foreign service supplier who has established a commercial presence in the country (the movement of capital). The service supplier may also bring in some foreign providers or managers – combining mode 3 with mode 4 – but the tendency is to use local service providers.

The WTO Secretariat states that commercial presence is "the most important mode of supply of services, at least in terms of future development," and that it "also raises the most difficult issues for host governments and for GATS negotiations."[71] That is because many services, for instance a medical treatment, generally require the service provider and recipient to be in the same place. Efforts and rules to liberalize trade via commercial presence, therefore, target the reduction or elimination of measures that restrict market access to foreign suppliers, or treat these suppliers differently from domestic ones. In other words, this form of trade directly challenges governments' domestic policies and measures.

UNCTAD[72] notes four categories of commercial presence in the health sector:

- in the hospital operation/management sector;
- in the health insurance sector;
- in the health/medical education sector; and
- in ad hoc arrangements (e.g. temporary presence in a developing country as part of a health development funding project).

UNCTAD also points out that there are many restrictions, or outright prohibitions, in most countries on foreign commercial presence in the health sector. Chief among them are economic and needs-based quantitative limitations; rules favouring local over foreign suppliers; restrictions on property acquisition; foreign investment restrictions; and prohibition of for-profit hospitals or foreign ownership of hospitals or other health facilities.

The United States is a prime example of both sides of the commercial presence coin. On the one hand, U.S. health care companies are major exporters of services via their foreign affiliates. Luther's[73] examination of health sector fundamentals in the United States found that American foreign affiliates averaged annual growth in sales of 25 percent between 1992 and 1995, but that sales plunged by 47 percent, or US$360 million, in 1996. This is attributed to several of the U.S. health care service providers refocussing their core business activities back in the U.S. domestic market (in two instances related to U.S. Department of Justice investigations of company practices). As an aside, the withdrawal of foreign suppliers from health sectors in other countries raises questions about the impact that such withdrawal may have on the host health system (e.g. in terms of its ability to meet health care needs).

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[71] WTO Secretariat, *Guide to Uruguay Round Agreements*, op. cit., 164.

[72] UNCTAD Secretariat, "International Trade in Health Services: Difficulties and Opportunities for Developing Countries," op. cit., 19.

There is also significant commercial presence of foreign affiliates in the U.S. health care market. In each year from 1992 to 1996, the United States purchased more health services from U.S.-based foreign affiliates than it sold abroad through the foreign affiliates of U.S. health services providers. In 1996, health services sales by foreign affiliates in the United States increased 126 percent to US$3.5 billion as a result of a couple of major acquisitions of U.S. health services companies. The foreign presence in the U.S. health services market was dominated in 1996 by companies based in Germany, Canada, Australia and Japan, in that order. In comparison, more than half of all health services sales by U.S. affiliates abroad were in the United Kingdom. Luther attributes the greater openness of the U.S. market to private provision of health services as being conducive to the establishment of foreign affiliates. U.S. firms, on the other hand, are hampered by the fact that many foreign governments control their health systems, or restrict the financing of private health sector services. Luther concludes, however, that the outlook for U.S. commercial presence abroad will likely improve as foreign governments allow a greater role for the private sector in their health care systems.

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[73] D.R. Luther, "Health Care Services: Strong Fundamentals and Innovations Foreshadow Growth in U.S. Exports and Foreign Direct Investment," op. cit., 21.

Managed care is a prominent U.S. health export. This is not surprising since most managed care companies are for-profit and, as their domestic markets shrink, they look abroad to maintain their economic bottom lines. The Economist Intelligence Unit[74] notes that there may not always be a good fit between the managed care approach and health systems in other countries, but there still remain merits in this approach for some other countries' financing, administration and delivery of health care. Managed care was seen as less exportable in countries with relatively low health spending, a shortage of specialists, weak data collection and management systems, and where employers are not a part of the health care process. Two examples given of international activity in the managed care field are BlueCross/BlueShield of Delaware in Taiwan and UnitedHealthcare Global Consulting in South Africa.

Industry predictions that managed care would make significant inroads in European health systems have not materialized. One spokesperson attributed this to the strength of lobbies (and of doctors in particular), technical difficulties related to implementation, and a debate that confused ideological (state vs. market) and technical (e.g. efficiency) issues. Other reasons cited were opposition to managed care, government regulation and the special status of health care in European countries.[75] Prime examples of this failure were attempts at "prescription by mail" (mail order pharmacies) and disease management plans. Export efforts by U.S. companies into Europe continue, and the strategy appears to have shifted from one of transplanting the U.S. model to one of focussing on selective elements of managed care that hold more promise of acceptance.

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[74] The Economist Intelligence Unit, "Profile – Is US-Style Managed Care Exportable?" *Healthcare International* (London: EIU, 1st Quarter, 1999): 46-56.

[75] The Economist Intelligence Unit, "Profile – An Uphill Struggle for Managed Care in Europe," *Healthcare Europe* (London: EIU, 3rd Quarter, 1999): 29-40.

Latin American countries (e.g. Argentina, Brazil, Chile, Mexico, Peru, Colombia, Ecuador, Guatemala, Panama, Venezuela, Uruguay) are also an export destination for U.S. and European managed care firms. According to Stocker et al.,[76] several factors are contributing to this: economic circumstances favourable for managed care (e.g. strong economic growth, small percentage of GDP spent on health, low private health insurance coverage); the presence of foreign multinational (principally American) companies that favour managed care plans for their employees; and loan conditions set by, for example, the World Bank and other lending bodies that favour privatization and less public spending. With the presence of managed care companies in Latin America, there is a growing concern that access to health care is suffering (e.g. co-payments to patients), and that resources that could be spent on health services are going toward administration costs and returns to investors.

The diffusion of managed care abroad is raising concerns about the impact on health services and health because of growing evidence of managed care's negative impacts in the United States. Faced with a profitability squeeze and increased competition, the U.S. managed care industry has pursued policies of cost containment, market consolidation and acquisitions. One major consequence of this market-driven health care, according to Kuttner,[77] is restrictions on services and care. He sums up his look at the industry this way:

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[76] K. Stocker et al., "The Exportation of Managed Care to Latin America," *The New England Journal of Medicine* (April 8, 1999): 1131-1136.

> In the early 1990s, entrepreneurs succeeded in obtaining the easily available cost savings, at great profit to themselves and their investors. By the late 1990s, however, pressure to protect profit margins had led to such dubious business strategies as the avoidance of sick patients, the excessive micromanagement of physicians, the worsening of staff-to-patient ratios, and the outright denial of care. In an industry driven by investor-owned companies, the original promise of managed care – a greater efficiency in the use of available resources and greater integration of preventive and treatment services – has often degenerated into mere avoidance of cost. (p. 668)

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[77] R. Kuttner, "The American Health Care System: Wall Street and Health Care," *The New England Journal of Medicine* (February 25, 1999): 664-668.

A backlash by patients and providers has developed in response to the industry's actions. Several states have attempted to protect patients through patients' rights legislation. In October 1999, the U.S. House of Representatives passed a bill to protect patients in managed care plans by making it easier for them to see a specialist, to obtain prescription medicines and care in hospital emergency rooms, and to sue health care providers for injuries suffered from being denied care.[78] California, Georgia and Texas now have legislation that allows patients to sue health plan providers for harm resulting from the denial of care.

Foreign commercial presence in the health sector is about privatization, albeit privatization with a difference – whether to allow foreign companies to finance and/or deliver health care services. Privatization in the health sector of a country is a necessary but not sufficient condition for foreign commercial presence (i.e. a country may allow privatization but prohibit foreign companies from its health sector). In the case of health systems, however, the fundamental issue is privatization, and not so much whether privatization is by domestic or foreign companies. That is not to deny the importance of issues concerning domestic versus foreign privatization ventures (e.g. different approaches to privatization by domestic and foreign companies).

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[78] J. Rovner, "US Government Strengthens Patients' Rights," *The Lancet* (Vol. 354, October 16, 1999): 1366.

As a mode of health services supply and trade liberalization, foreign commercial presence fits squarely in the debate about public/private health care in health policy. Not surprisingly, arguments for both privatization and foreign commercial presence are similar (e.g. better cost control, improved efficiency and quality of care and services). The evidence, however, generally does not support these arguments. The case of managed care has already been mentioned. In their study of Australia's hospital sector, White and Collyer[79] found that, with the growth of foreign and local corporate investment, "the capacity of the state to plan, coordinate, and manage the health care sector is being steadily eroded, as is the capacity of the profession to act in the interests of patients and the public at large." (p. 506) With private ownership, the goals of efficiency and profit dominated at the expense of health objectives concerning equity, access, quality of service, and public accountability. Barraclough[80] expresses similar concerns about the situation in Malaysia, which has a growing private hospital sector supported by foreign companies and the government's own investments in private hospitals.

A fuller discussion of the public/private issue is, however, beyond the scope of this paper. Technical and ideological dimensions of this debate can be found in the health policy literature, including recent books by Drache and Sullivan[81] and Tuohy.[82]

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[79] K. White and F. Collyer, "Health Care Markets in Australia: Ownership of the Private Hospital Sector," *International Journal of Health Services* (Vol. 28, No. 3, 1998): 487-510.

[80] S. Barraclough, "The Growth of Corporate Private Hospitals in Malaysia: Policy Contradictions in Health System Pluralism," *International Journal of Health Services* (Vol. 27, No. 4, 1997): 643-659.

The question remains, however, that if the advantages of privatization are so evident, why is it that most industrialized countries, with the notable exception of the United States, have health care systems that are predominantly publicly financed, provide universal coverage, and tend to achieve better outcomes on health status, efficiency and cost control? In their study of OECD countries, Anderson and Poullier[83] found that in the United States health spending, both in GDP and per capita terms, was higher; the rate of growth in spending was more rapid; the percentage of the population insured for health was lowest; hospital days per capita were fewest; hospital expenditures per day were highest; physician incomes were higher; and outcome measures were in the lower half of all countries in the study.

Finally, there may be some irony in the relationship among trade liberalization, free markets and economic development. Health expenditure data indicate that as countries' incomes increase, the share of total health spending by the public sector increases.[84] This is attributable to the higher revenue base of governments, as well as their choice to use public rather than private financing to address market failures in the health sector. This reinforces the point made by the WHO, cited earlier in this paper. Countries that have benefited most from market mechanisms to achieve their higher levels of development are the same countries that rely upon government financing in the health sector to achieve such objectives as equity and access.

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[81] Drache and Sullivan, *Market Limits to Health Reform: Public Success, Private Failure,* op. cit.

[82] Tuohy, *Accidental Logics: The Dynamics of Change in the Health Care Arena in the United States, Britain and Canada,* op. cit.

[83] G.F. Anderson, J.-P. Poullier, "Health Spending, Access, and Outcomes: Trends in Industrialized Countries," *Health Affairs* (May/June 1999): 178-192.

[84] G. Schieber and A. Maeda, "Health Care Financing and Delivery in Developing Countries," *Health Affairs* (May/June 1999): 193-205.

Mode 4: presence of natural persons

The supply of health services under the GATS mode 4 means that a foreign service supplier crosses into another country to provide services (i.e. the movement of labour). This may be in conjunction with foreign commercial presence (i.e. where the foreign establishment hires foreign service providers), or where the foreign provider is an employee of a foreign service company, or where the service provider is acting alone. A key point to note is that this GATS mode of trade liberalization is limited to the temporary movement of labour. Mobility associated with citizenship, residence and employment on a permanent basis is excluded. The GATS, however, neither defines the meaning of temporary presence nor specifies a time frame that applies to the term "temporary."[85]

According to UNCTAD, this form of trade in health services is significant because of the labour-intensive nature of health services, shortages of health human resources in many countries, and the more or less universal scientific knowledge upon which health services are based.[86] It notes that the flow of physician labour has, over time, changed from a situation where the supply came mainly from developed countries to one where developing countries are now a significant supplier. UNCTAD reports that 56 percent of all migrating doctors come from developing countries, but only 11 percent go to these countries. The difference may be even larger for nurses.

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[85] WTO Council for Trade in Services, *Presence of Natural Persons (Mode 4)*, S/C/W/75 (Geneva: WTO, December 1998).

[86] UNCTAD Secretariat, "International Trade in Health Services: Difficulties and Opportunities for Developing Countries," op. cit., 6.

"Rich" countries have been criticized by Kirsten Stallnecht, President of the International Council of Nurses, for using their "pseudo-shortages" of nurses to recruit nurses from developing countries.[87] According to Stallnecht, a root cause of shortages in developed countries is human resource policies that lead nurses to leave the profession. Better policies to retain nurses, for example, would solve such pseudo-shortages. Instead, developed countries are recruiting nurses from developing countries whose health care will suffer as a result of the loss of nurses.

UNCTAD also notes a significant trend of the lowest-income countries having difficulties replacing their lost health human resources. For example, South Africa has experienced a loss of doctors both to out-migration to developed countries, and to the private health sector at home. Faced with a shortage of physicians, South Africa has had to rely upon arrangements with neighbouring and more distant countries to meet needs for medical personnel. Situations like this in the developing world raise concerns about the consequences of the loss of needed health human resources on health outcomes and health systems in these countries.

More and more countries are facing health human resource shortages. For example, Japan's need for an increasing number of nurses to care for an ageing population may lead to changes in that country's visa and residency regulations to permit foreign nurses to work there.[88] This easing of policies to allow foreign nurses would be a significant development in a country where foreign residents represent a relatively small percentage of the population. Norway, Sweden as well as the United Kingdom, Ireland and France are all looking to Germany's physician surplus as a possible source for doctors to meet their own supply shortages.[89] In Canada, both the Canadian Nurses Association and Canada Medical Association have raised concerns about shortages in their respective fields and the impact on the health system.

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[87] A. Picard, "Brain Drain Hurts World Health: Expert," *The Globe and Mail* (June 21, 2000).

[88] J. Lamar, "Japan to Allow in Foreign Nurses to Care for Old People," *British Medical Journal* (Vol. 320, March 25, 2000), 825.

A recent Statistics Canada study[90] found that the health professions were most affected by the "brain drain" of knowledge workers to the United States. For instance, in 1996 and 1997, permanent emigration relative to the stock of workers in Canada was highest for doctors and nurses; in the 1990s there were 19 physicians and 15 nurses leaving Canada for every physician and nurse entering the country; and the annual loss of doctors and nurses has been high relative to the supply of new graduates in these professions (equivalent to about 25 percent of the number of new graduates). In contrast, a lower labour market demand for health professionals in the 1990s led to a decline of 40 percent and 70 percent, respectively, in the immigration to Canada of doctors and nurses.

According to Adams and Kinnon, the temporary movement of health human resources across national borders has potential significance for access to health care, the quality of care and efficiency of the health sector.[91] In the originating country, emigration that results in shortages of needed health human resources can mean reduced access to care, for example, in terms of what services may be available, or the time it takes to access services. Quality of care may suffer from a loss of highly skilled and experienced providers, and efficiency will be reduced in a system that spends public funds to educate and train health human resources only to have them leave.

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[89] K. Birchard "Germany's Surplus of MDs the First Stop in Attempt to Fill Shortages," *The Medical Post* (May 2, 2000), 55.

[90] J. Zhao, D. Drew and T.S. Murray, "Brain Drain and Brain Gain: The Migration of Knowledge Workers from and to Canada," *Education Quarterly Review* (Statistics Canada, Catalogue no. 81-003, 2000, Vol. 6, No. 3): 8-35.

[91] O. Adams and C. Kinnon, *Health Economics Technical Briefing Note: Measuring Trade Liberalization against Public Health Objectives: The Case of Health Services*, op. cit.

The opportunities and costs of labour mobility to a country's health system will depend upon a combination of factors including the health needs of the population (e.g. changing population demographics), the health human resources situation in the country (e.g. supply, demand and distribution), and policy and program reforms in the health system (e.g. shift in care from hospital- to community-based services). Also, the labour-intensive nature of health services means that labour costs are one of, if not *the*, major cost factors faced by health systems. This fact, and its links to labour inflows and outflows, is not lost on governments that fund such services and need to contain costs as part of keeping health systems sustainable.

Being the originating or recipient country of labour movements is also important for health systems, as noted earlier, but also more generally. Originating countries may risk a loss of domestic resources and transfer of educational investment, but benefit from experiences brought back by those who went abroad temporarily, and from remittances sent home by persons working abroad. For recipient countries, the temporary movement of labour can help to address labour shortages and provides access to providers at lower overall investments (e.g. training costs borne by the originating country).[92]

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[92] WTO Council for Trade in Services, *Presence of Natural Persons*, op. cit.

Several measures can affect the cross-border movement of labour. UNCTAD[93] mentions the following:

- economic needs tests (e.g. the need/demand for the service; whether the service can be supplied locally);
- licensing, accreditation, certification, and the recognition of foreign qualifications;
- requirements on nationality and residency;
- particular subnational (i.e. provincial or state) requirements;
- immigration requirements;
- access to exams for meeting qualifications; and
- discriminatory regulation of fees and expenses.

The European Union presents one example of difficulties associated with the freer movement of labour. In the EU, employment legislation regarding mutual recognition of professional qualifications is intended to improve the labour mobility among countries, including the cross-border movement of health care workers with diplomas as medical professionals, general care nurses or in pharmacy[94] Labour mobility, however, has been limited due to, among other reasons, bureaucratic difficulties and the need for fluency in the host country's language.

According to the WTO,[95] few members made comprehensive GATS commitments to liberalize the movement of labour under market access and national treatment. Adlung[96] attributes this to political and economic sensitivities about having foreign service providers physically present in their territories. The health sector reflects this general pattern where few WTO members liberalized services trade based on the movement of labour. In the case of professional services (physicians, dentists, midwives, nurses, physiotherapists and paramedical personnel), Butkeviciene and Diaz[97] found that the majority of scheduled commitments on market access and national treatment were "unbound" (i.e. no commitment to liberalize – the country remains free to introduce trade-restrictive measures). Nationality and permanent residency requirements, as well as requirements for permits, authorization, and registration or membership in professional associations were measures restricting the movement of professionals. This situation of limited trade liberalization also applied to hospital and other health services. The health services sector, then, saw little mode 4 trade liberalization in the first round of GATS.

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[93] UNCTAD Secretariat, "International Trade in Health Services: Difficulties and Opportunities for Developing Countries," op. cit.

[94] V. Kendall, *The Prospects for Private Healthcare in Europe*, op. cit.

[95] WTO Council for Trade in Services, *Presence of Natural Persons*, op. cit.

[96] R. Adlung, "Services Trade Liberalization from Developed and Developing Country Perspectives," in P. Sauvé and R.M. Stern (eds.), *GATS 2000: New Directions in Services Trade Liberalization* (Washington, D.C.: The Brookings Institution, 2000), 112-131.

Conclusion

Despite the occurrence of international trade in health services, few WTO members agreed to binding commitments to liberalize trade in health services in the Uruguay Round. In fact, only education services saw fewer WTO members make liberalization commitments. WTO services data[98] for 122 WTO members on specific commitments to liberalize trade in health services show that:

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[97] J. Butkeviciene and D. Diaz, "GATS Commitments in the Health Services Sector and the Scope for Future Negotiations," in Zarrilli and Kinnon, *A Development Perspective*, op. cit., 135-158.

[98] Europa, European Union website, "Opening World Markets for Services: Legal Texts and Commitments" (http://gats-info.eu.int/inex.html).

- 35 members (29 percent of the WTO membership) made commitments on medical and dental services;
- 12 members (10 percent of the WTO membership) made commitments on the services of midwives, nurses and physiotherapists;
- 27 members (22 percent of the WTO membership) made commitments on hospital services; and
- 12 members (10 percent of the WTO membership) made commitments on other human health services.

No commitments were made by Canada in any of the above GATS health services categories. With the exception of limited commitments for hospital services, the United States was also non-committal. Commitments were made by the EU on the following services: medical and dental; midwives, nurses, physiotherapists; and hospital. In many cases, however, restrictions were put on the commitments to liberalize trade (e.g. no commitment on the mobility of labour; market access of professionals being restricted to natural persons, and made subject to economic needs tests, supply factors such as shortages of doctors and manpower planning factors, nationality and annual quotas; and market access to hospital services limited by health services plans, needs tests and prior authorization).

Butkeviciene and Diaz[99] are of the view that there have not been any policy implications for WTO members that made GATS commitments on health services because those commitments reflected the status quo and excluded sensitive areas.

The paucity of commitments on health services reflects the wider failure of the Uruguay Round to achieve substantial liberalization in services trade more generally. Some attribute this failure, in part, to weaknesses in the conceptualization and design of the GATS that created too much flexibility and scope for countries to maintain existing protective trade measures (e.g. not enough transparency, an approach to liberalization based on sectors and modes of supply, conditional obligations).[100] [101] [102] Another problem, noted by Feketekuty,[103] is a lack of clarity and user friendliness in the GATS – something sure to induce caution, if not reluctance, on the part of negotiating countries.

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[99] J. Butkeviciene and D. Diaz, "GATS Commitments in the Health Services Sector and the Scope for Future Negotiations," op. cit., 135.

Weaknesses in the GATS architecture may have played some part in the fact that most countries did not liberalize trade in health services. But undoubtedly more was at play in the defensive positions adopted. For services in general, there was a tendency for a country's income and its GATS trade liberalization to be directly related (i.e. higher-income countries scheduled more service sectors for liberalization).[104] That relationship doesn't appear to hold for health services. Why? As noted earlier in the paper, higher-income countries tend to have health care systems with universal insured coverage and largely state financing. This may explain two possible key reasons why these countries have not undertaken substantial trade liberalization. First, these countries may consider their public health services to fall outside the GATS definition of services and, therefore, not be subject to trade negotiations (according to GATS Article I (3)(b)(c), "services supplied in the exercise of governmental authority" are not considered services for GATS purposes). Second, the choice of a public health care system characterized by universal coverage and equitable access to services reflects an approach to health care as a public good rather than a market or tradable commodity. In this case, commercial activity through trade liberalization in health services would be seen as incompatible with the nature of the good.

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[100] R. Adlung, "Services Trade Liberalization from Developed and Developing Country Perspectives," op. cit.

[101] B. Hoekman, "Assessing the General Agreement on Trade in Services," op. cit.

[102] P. Sauvé, "Assessing the General Agreement on Trade in Services: Half-Full or Half-Empty," *Journal of World Trade* (Vol. 29, 4, 1995): 125-145.

[103] G. Feketekuty, "Assessing and Improving the Architecture of GATS," in P. Sauvé and R.M. Stern (eds.), *GATS 2000: New Directions in Services Trade Liberalization* (Washington, D.C.: The Brookings Institution, 2000), 85-111).

[104] B. Hoekman, "Assessing the General Agreement on Trade in Services," op. cit.

Countries with public health care systems were not the only ones, however, to limit or abstain from liberalizing health services. A most obvious example is the United States. Despite its predominantly private health care system, and a role in the Uruguay Round as one of the main "instigators, facilitators and mediators,"[105] the United States undertook limited trade liberalization in its health sector.

In conclusion, the expansion of international trade is inevitable, and there will be increasing pressure to liberalize trade in health services through multilateral trade agreements such as the GATS. A better understanding of international trade and health services is hampered by an absence of detailed data, information and knowledge. There is a real need for the health policy and research communities to help develop the information, knowledge and understanding needed for informed decision making in this area. This present overview of international trade and health suggests that the issues are complex and the stakes high.

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[105] R. Adlung, "Services Trade Liberalization from Developed and Developing Country Perspectives," op. cit.

Trade and the Environment: Post-Seattle Looking Forward

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The opinions expressed in this document are those of the author and do not necessarily reflect the opinions of the Government of Canada or Environment Canada.

Introduction

The trade and environment policy interface is about good governance. It is about trade governance in an integrated global market, and about sound environmental stewardship in an equally integrated, if not more so, physical environment. Moreover, trade governance and environmental stewardship have the same goal – a high quality of life. The difference is that trade is very much a means, while the environment is a means and an end.

This paper provides an overview of the debate on trade and environment in a multilateral context, and highlights the diversity of the issues and challenges involved. The paper has two parts: an overview of the trade and environment interface; and some views on a way forward in the wake of the World Trade Organization (WTO) Ministerial meeting held in Seattle in December 1999.

An Overview of the Debate

Increasing interdependence

For a considerable number of years, global trade and foreign direct investment growth have increased at a faster rate than growth in overall economic activity. This has resulted in a transformation of the global economy from a state of essentially *independent* economies, trading a relatively small share of their domestic production, to a situation where economies are essentially *interdependent,* trading a larger share of their domestic production. At the same time, reflecting the fragmentation of production across borders due to the vast expansion of foreign direct investment, the global economy has evolved from what has been termed a model of "shallow integration" to a model of "deeper integration."

As a result, trade policy has become a more important element of economic policy overall, and the focus of trade policy has shifted from the tariff and other border measures to issues such as subsidies and government procurement practices, which were traditionally seen as purely domestic but which are now increasingly giving rise to trade frictions.

Coinciding with this trend, at least in the developed countries, has been a greater political interest in the relationship between economic policy and regulation in other policy spheres, including environmental policies and regulations.[1] In an international context, the trade-environment linkage has been on the international agenda in various forums, particularly following the 1992 UN Conference on Environment and Development.

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[1] A recent U.S. poll is revealing. When asked what should be a major priority of U.S. trade agreements, a large majority of respondents said protecting the environment (80 percent major priority, 14 percent minor priority). By comparison, with respect to keeping foreign markets open to U.S. exports, 56 percent saw this as a major priority and 32 percent as a minor priority. So at least in the United States, there are indications that the public considers trade agreements significant environmental instruments. Source: *Business Week,* April 24, 2000.

The linkages between trade and the environment

The public's general concern has been that, through adverse effects on the environment (in terms of increasing pollution, accelerating resource depletion and contributing to the erosion of the environmental legacy), trade lowers the overall quality of life for both present and future generations. Addressing this concern in an objective manner may well be key to maintaining public support for an open trading system and building support for a strengthened and more open multilateral trading system, including investment.

Assessing how trade or changes in trade policy impact upon and influence environmental conditions is not, however, a simple matter or without inherent uncertainties. Krueger and Grossman have outlined three mechanisms through which trade and foreign investment policy can affect the level of pollution and the rate of resource depletion. These mechanisms are the *scale effect* (where an increase in trade and investment liberalization leads to an expansion of economic activity), the *composition effect* (where liberalization leads to a change in the composition of products that an economy produces), and the *technique effect* (where technological change is associated with trade and investment).[2] The Organization for Economic Co-operation and Development (OECD) has provided a still finer taxonomy of effects (breaking out product effects, technology effects, regulatory effects, scale effects and structural effects); and the NAFTA Commission on

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[2] G.M. Grossman and A.B. Krueger, "Economic Growth and the Environment," *Quarterly Journal of Economics* (1995).

Environmental Co-operation (CEC) has also developed methodologies for assessing trade-related environmental effects.[3]

Some of the trade-environment interactions are direct, such as the import and export of environmentally friendly or hazardous products. Others are indirect, such as the positive influence of trade on per capita incomes, which in turn stimulates demand for a cleaner environment, or the positive impact of trade on the level of economic activity, which in turn creates pollution.

When assessing the impact of trade on the environment, the quality of environmental policy must, however, also be considered. When environmental policies are not set appropriately, trade and investment can indeed serve to aggravate environmental problems. However, in a context of sound environmental policies, available evidence suggests that trade and investment usually will have a positive impact on the environment.[4]

For example, if domestic prices for products are distorted, such as through subsidies, trade and trade liberalization may have an adverse environmental impact. In this regard, a World Bank report concluded that "Some government polices are downright harmful for the environment. Notable here are distorted prices in general and subsidized input prices in particular."[5] Subsidies to producers or consumers of energy and agricultural products have been identified as particularly damaging to the environment in that they encourage excessive use of fossil fuels, irrigation water, pesticides and logging. The Worldwatch Institute has also documented how subsidies for such activities as mineral production, logging, fishing, agricultural inputs and production, and energy use have contributed to a range of environmental problems.[6]

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[3] See Commission on Environmental Co-operation, *Assessing the Environmental Effects of the North American Free Trade Agreement (NAFTA)* (Montreal: CEC, 1999); and Organization for Economic Co-operation and Development, *Methodologies for Environmental and Trade Reviews* (Paris: OECD, 1994). Both organizations have ongoing work programs in these areas.

[4] A similar argument may be made regarding the impact of economic growth on the environment: in a context of weak environmental policy, growth can damage the environment, but well-framed environmental policies can lead to environmental improvements from economic growth. And let us not forget that lack of economic growth, or a collapse in trade, can contribute to environmental degradation, although this observation is less often made – at least publicly – by critics of the WTO.

This, however, does not imply that trade or trade liberalization should be avoided, nor that trade measures are the most appropriate response to subsidization of resource use.[7] Rather, an appropriate domestic environmental policy, crafted to internalize environmental costs, is required to avoid negative environmental impacts. The reduction or elimination of these types of subsidies promotes efficient use of resources, with beneficial effects for the environment as well as for trade.

The linkages between foreign direct investment and the environment

The general public concern regarding the impact of foreign direct investment (FDI) on the environment reflects the fear that differences in environmental standards will promote the relocation of firms to economies with lower effective environmental standards (i.e. "pollution havens") and result in a race to the bottom for environmental standards.

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[5] World Bank, *World Development Report* (Washington: World Bank, 1992), p. 11.

[6] David Malin Roodman, "Reforming Subsidies," in Lester R. Brown et al., *State of the World 1997* (New York: W.W. Norton & Company, 1997).

[7] For a discussion on some of the difficulties of using countervailing duties in response to "environmental subsidies," see Robert T. Stranks, *Pandora's Box?: Countervailing Duties and the Environment* (Ottawa: Department of Foreign Affairs and International Trade, October 1994).

The OECD has made several observations in response to this fear.[8] First, there is little empirical evidence indicating that countries lower their environmental standards in order to attract so-called "dirty" industries. Second, there is not much evidence of firms relocating to countries with lower environmental standards in order to take advantage of the lower standards. While firms do move from high- to low-standard countries, the reasons for doing so usually have little to do with environmental standards in either country. Very few firms undertake foreign investment with reduced environmental compliance costs as their primary objective.

This said, as the study notes, the *threat* of industrial relocation is often used by firms who would like to have the burden of environmental policies reduced. Thus, "the threat of industrial migration based on 'pollution havens' (rather than the reality of this migration) may be generating a 'political drag' on environmental policy-innovations in OECD countries."[9]

Summing up the evidence

Accordingly, there is no simple one-to-one mapping between growth in trade and economic activity on the one hand and changes in the environment on the other. Indeed, trade and trade liberalization can relate to the environment in four ways:

1) absolutely beneficial for the environment;
2) neutral in respect to the environment;
3) negative for the environment, but less negative than the same level of economic growth or developments that would

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[8] Organization for Economic Co-operation and Development, *Economic Globalisation and the Environment* (Paris: OECD, 1997).

[9] Ibid., p. 13.

occur over time in the absence of trade or trade liberalization; and

4) more environmentally negative than the same level of economic growth or developments that would occur over time in the absence of trade or trade liberalization.

While (1) is clearly the preferred outcome, (2) or (3) should also be acceptable from an environmental as well as trade perspective, other things being equal.

The key to this relationship would appear to be technology. International diffusion of technology and the use of efficient (resource-saving) products can be facilitated by freer trade and liberal investment policies.[10] FDI and technology transfer also imply that the links between trade and the environment need to be considered in a long-run framework.

As a matter of global public policy and policy coherence, two points need to be emphasized. First, trade policy (which promotes liberalized trade and investment) and environmental policy (which promotes a high-quality environment) share the common objective of improving living standards. Second, to achieve this objective, co-operation is required because of the interdependence of countries on both of these issues. Furthermore, the challenges of sustainable development are considerable even with maximum co-operation.[11]

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[10] John Begin and Michel Potier, "Effects of Trade Liberalisation on the Environment in the Manufacturing Sector," in *The World Economy*, 20, no. 4 (July 1997).

[11] In Canada's case, policy coherence is reflected in the aim to ensure that trade rules provide the necessary flexibility to implement effective environmental policies while maintaining the integrity of the multilateral trading system. Canada is generally committed to integrating sustainable development into domestic and foreign policy. With respect to trade and environment, Canada's objectives are as follows: (1) to ensure governments can implement effective environmental laws and policies while preserving the integrity of the rules-based multilateral trading system; (2) to ensure that Canada's environmental policies minimize any adverse trade effects; and

Looking Forward

Addressing the trade and environment interface in the post-Seattle WTO Ministerial environment will be a challenge, both in terms of developing domestic public support and in terms of developing an international consensus to move forward. Any Canadian strategy to confront this challenge must take into account that Canada (a) is integrated into the global economy and multilateral trading system; (b) has important environmental interests both domestically and in terms of the global commons; (c) is party to a number of international environmental agreements; and (d) is party to an already existing dynamic international environmental "architecture." Importantly, as events surrounding the Seattle Ministerial vividly illustrated, the strategy must, in its design and implementation, be fully open, with an ongoing dialogue maintained with Canadian civil society in addition to traditional stakeholders. Lastly, and most importantly, the trade and environment agenda must take into account the development aspirations of the developing countries if there is to be any real prospect of arriving at a satisfactory outcome.

One way forward might be characterized as a "WTO-plus" approach. This approach places trade and environment issues into three categories: those that need to be addressed within the WTO; those that involve co-operation between the WTO and other international institutions; and those that can be addressed outside the framework of the WTO.

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(3) to promote sound environmental practices and improve market access for environmental goods and services.

WTO members have made an explicit commitment to sustainable development and the protection of the environment. This commitment is enshrined in the preamble to the WTO Act. Thus, while not being an environmental organization nor being charged with administering any specific substantive agreement dealing with the environment, the WTO supports the concept of sustainable development and recognizes that there are linkages between trade and environmental issues. As well, at the Seattle Ministerial, the developing countries stressed that development was also an inherent consideration in multilateral trade negotiations.

Upon its establishment on January 1, 1995, the WTO created the Committee on Trade and Environment (CTE) to pursue a work program on trade and environment issues set out in the Marrakech Decision.[12] To address its mandate in a systematic manner, the CTE has adopted the so-called "cluster approach." The first cluster consists of items relevant to the theme of market access, and the second cluster consists of items related to the linkage between the multilateral environment agenda and the multilateral trade agenda.

The issues of particular interest to Canada that are currently being discussed in the CTE are as follows:

- *Multilateral Environmental Agreements (MEAs):* Canada supports further work in the CTE to clarify the relationship between WTO rules and trade measures in the MEAs. While no MEA has been challenged to date in the WTO, this provides little comfort for the future. Canada has proposed a "principles and criteria" approach to clarify WTO rules. Such an approach would assist WTO panels in assessing trade measures contained in MEAs, and assist those developing MEAs in constructing WTO-consistent trade measures.[13]

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[12] WTO Trade and Environment Decision of April 14, 1994.

- *Eco-labelling:* Canada supports eco-labelling on a voluntary basis but seeks to avoid the risk inherent in mandatory schemes of their becoming hidden trade barriers. Within the CTE, Canada supports further discussion of non-product processes and production methods (PPMs) with respect to voluntary standards.
- *Market Access:* Canada supports liberalization of trade in environmental goods and services on the grounds that the technology that they embody would enhance the ability of countries around the world to deal with environmental challenges.
- *Subsidies:* The CTE has had some initial discussions on subsidies. It is widely acknowledged that there are potential environmental benefits from removing trade restrictions and distortions in a number of sectors, such as agriculture, energy and fisheries. For example, trade-distorting subsidies to the fishing sector also contribute to a build-up of excess capacity and undermine the sustainable use of marine resources. Particular aspects of subsidies will be negotiated as part of the WTO's "built in" agenda, for example the "green box" in the agricultural sector, but a broad-based discussion of subsidies in an environmental context would be appropriate for the CTE.

Other environment-related issues that may be appropriate for a CTE with a broadened mandate to consider are:

- *The Application of Precaution:* The application of precaution, which is often expressed by the terms "precautionary principle" and "precautionary approach," is particularly relevant to the WTO's Agreement on

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[13] It should be noted that while this activity is within the WTO, it involves inter-institutional co-operation.

Sanitary and Phytosanitary Measures (SPS Agreement). The SPS Agreement recognizes the legitimate right of governments to maintain the level of health protection they deem appropriate but ensures at the same time that the right is not abused and does not result in unnecessary barriers to trade. The Agreement explicitly recognizes the right to take precautionary provisional measures when scientific evidence is lacking, while seeking further information.

- *Processes and Production Methods:* Article III of the General Agreement on Tariffs and Trade (GATT), which provides for "national treatment," precludes discriminatory treatment of imports compared to domestic products – including discrimination based on PPMs used in the product's development. Since different PPMs have varying environmental consequences, the question arises from an environmental perspective as to whether countries *should* be able to treat products differently (including the right to impose import restrictions) on the basis of PPMs. This is a highly contentious issue, given the difficulty of distinguishing "beggar-thy-neighbour green protectionism" from environmental protection. This issue, and others such as subsidies, could also be linked to MEAs.
- *Trade and Foreign Investment:* The question of whether a framework of multilateral rules on foreign investment should be established in the WTO is a contentious issue. This, however, does not alter the fact that there are significant relationships between foreign investment, trade and the environment. Most notable is the impact of foreign investment on economic growth and development.

The CTE's progress in advancing its work program has been, in the view of some observers, somewhat less than sterling, leading them to conclude that high-level multilateral and bilateral discussions are needed to elicit real commitment to integrating trade and environment concerns, and to bringing economic development considerations into the equation for a sustainable development approach.[14]

Outside of the CTE, there are three possible ways to advance the environmental agenda within the WTO.

First, environmental considerations could be included in the negotiations on agriculture and services trade that, as per the "built-in agenda" of the Uruguay Round, commenced in 2000. In developing its position for the Seattle Ministerial, Canada announced that it would indeed seek to ensure that environmental considerations are fully taken into account, at least in the context of Canadian participation in the negotiations. There is, however, a wide range of views amongst WTO members on having environmental issues explicitly reflected in these negotiations.

Second, trade and environment could be addressed in Trade Policy Review Mechanism (TPRM) reviews of WTO members' trade policies and performance. This mechanism has three broad objectives: first, to increase the transparency and understanding of members' trade policies and practices, through regular monitoring; second, to improve the quality of public debate on issues; and third, to enable a multilateral assessment of the effects of policies on the world trading system. From an environmental perspective, the first two of these objectives in particular could contribute to trade and environment transparency objectives. For WTO members such as Canada that undertake a trade-related environmental assessment or environmental review, the environmental component in a TPRM exercise would parallel their national initiatives and serve to demonstrate to the public that environmental issues are being taken into account in developing their negotiating positions, and that trade liberalization can contribute to sustainable development.[15] However, to be broadly acceptable in the current international political climate, the inclusion of environmental considerations in a TPRM might have to be made optional for each WTO member. The review of the operation of the TPRM mandated in the built-in agenda of the Uruguay Round affords an opportunity to address this idea.

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[14] In December 1996, the CTE's report to the first WTO Ministerial in Singapore demonstrated progress in terms of the WTO's recognition of the legitimacy of environmental policies. However, the report was disappointing from an environmental point of view in that there were few, if any, concrete steps toward integrating the environment into trade rules. The primary reason for the lack of results in the report to Singapore was a polarization between developed and developing countries. The latter view trade and environment as an issue that can only hurt them, in the sense of legitimizing the use of environmental measures as non-tariff barriers limiting their exports. They were therefore not interested in clarifying or modifying trade rules in such a way as to provide greater flexibility for environmental measures. This situation has not really changed since Singapore.

Third, and complementary to the outreach work being done within the CTE, Canada and a number of other WTO members support further outreach efforts by the WTO. Increased transparency of WTO operations, including more outreach by the Secretariat, would help maintain and build public support for the multilateral trading system. Canada has put forward a proposal on transparency and in particular noted the need for a regular budget to fund WTO outreach activities and for faster de-restriction of documents. Canada also believes that WTO members have a responsibility to inform their domestic stakeholders with respect to the WTO negotiations and provide adequate opportunities for consultation.

Given the public's interest in the WTO, and the criticism by some of the organization, increased transparency and outreach to promote understanding of the complexities of the trade and environment linkage is desirable.

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[15] For example, Canada's environmental review of WTO trade agreements and negotiations is a fundamental and publicly visible component of the trade strategy. In preparation for the Environmental Review, the Department of Foreign Affairs and International Trade released a paper entitled *Retrospective Analysis of the 1994 Environmental Review of the Uruguay Round* (Ottawa: November 1999).

With the WTO

The prime area where an inter-institutional approach is warranted is in clarifying and managing the relationship between MEAs and the WTO. The potential for MEAs and the WTO to come into conflict over the use of trade measures cannot be resolved in either environmental institutions or the WTO. A joint approach is required.

A second general area where inter-institutional co-operation would clearly be warranted is in research and analysis. In this regard, the OECD's analytical work on methodologies for the environmental assessment of trade liberalization is an example of where inter-institutional co-operation with the WTO has been recognized as contributing to moving the trade and environment agenda forward. In general, links between the OECD and WTO allow the greater analytical capacity of the OECD to be made available to, but the results and analysis not imposed upon, the members of the CTE. Other international bodies such as the United Nations Development Program (UNDP) and the United Nations Conference on Trade and Development (UNCTAD) also have a useful role to play in assisting the CTE in increasing its understanding of integrating environmental and sustainable development concerns into the multilateral trading system. In this regard, the WTO and the United Nations Environment Program (UNEP) have already concluded a co-operation agreement on trade and environment. One example of where future inter-institutional work will be required is to more fully understand the relationships and implications of the Kyoto Protocol and, more broadly, the potential linkages between trade and possible trade measures with climate change.

One suggestion for advancing the agenda has come from the International Institute for Sustainable Development (IISD) and the World Conservation Union (IUCN). The IISD and IUCN have proposed the convening of a Standing Conference on Trade and Environment (SCTE), whose aim would be to promote coherence in environmental policy as it relates to trade. The Conference would consist of the key environmental actors with an interest in trade policy, such as intergovernmental organizations and key elements of civil society, and seek to formulate practical recommendations for consideration in the WTO and other policy forums. In terms of logistics, the SCTE could function as an ongoing network with an annual conference.

Finally, to enhance its credibility and effectiveness, the WTO needs to be open to input from, and to maintain an ongoing dialogue with, environmental experts and a number of other international organizations. To its credit, the WTO has been engaged in this type of activity and the CTE has granted observer status to a number of international organizations including the International Monetary Fund (IMF) and World Bank. The WTO has also sponsored symposia on trade and the environment that have involved many civil society organizations (CSOs). These initiatives are consistent with the preamble of the WTO to ensure that the multilateral trading system is responsive to environmental and sustainable development concerns.

Outside the WTO

Enhanced international environmental co-operation and strengthened international environmental institutions could lessen the potential for conflict between trade and environment policies, quite independently of any direct involvement of the WTO. This could take a number of forms.

The most straightforward way would be to ensure effective implementation of the existing MEAs through enhanced support for capacity building and enhanced compliance mechanisms. Improved capacity-building provisions in MEAs would both make it more attractive for developing countries to support them and would improve the effectiveness of the MEA once it had been negotiated. Enhanced compliance mechanisms in MEAs would likely lessen the likelihood of trade-related MEA disputes being taken to the WTO rather than being resolved in the MEA. The real instruments and attractiveness of MEAs for developing countries would be the promotion of financial, technical and human resource capacities. This would make it attractive to become parties to the MEA and avoid undesirable environmental and economic competitiveness consequences.[16]

A second way would be to negotiate additional MEAs. Currently, MEAs are limited to a few specific trans-boundary or global environmental problems of particular concern. However, new MEAs on, for example, processes and production methods, could reduce the widespread concern within the environmental community that trade liberalization will exacerbate competitiveness-driven pressures for lower environmental standards. It would also be worthwhile to examine what steps the international community could take to raise international environmental standards more generally – although here it must be recognized that MEAs have their own limitations, and that environmental standards will for a number of reasons vary across countries, so some flexibility will be necessary.

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[16] In addition to considering capacity-building programs within the international environmental institutions, there is a need to consider the trade and development interface in a broader context and, in particular, the role that official development assistance can play in helping developing countries face trade and development challenges. In this regard see Kerry David Max, "Addressing Trade-Related Development Needs: Options for the Donor Community" in the present volume, which provides a number of suggestions for the overall co-ordination of trade-related development assistance.

Third, international institutional capacity and co-operation for the advancement of sustainable development can also be strengthened quite independently of the WTO.[17] Increased coherence and co-operation among international institutions such as UNEP and UNDP, UNCTAD, WTO, the World Bank, etc., would serve to enhance global environment-economy integration. While capacity building in environmental policy does not directly impact on multilateral trade rules, it does play a significant role in determining what the environmental effects of actual trade flows will be. And the environmental impact is an important variable in the public's assessment of the cost and benefits of trade liberalization, and consequently support for, or hostility toward, the multilateral trading system.

Illustrative of this approach is the UNCTAD and UNEP initiative to establish a Capacity-Building Task Force for Trade, Environment and Development (CBTF).[18] The initiative is being driven by demand from developing countries as well as by the desire to co-ordinate the organizations' various trade- and environment-related activities. The overall purpose of the CBTF will be to strengthen capacity, particularly within developing countries and economies in transition, to effectively address trade-environment-development issues. It is intended that the CBTF undertake a number of activities such as thematic research, country studies, training, policy dialogue and networking and information exchange.

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[17] The recent Malmo Ministerial Declaration reflects a growing view that a lack of coherence and co-ordination among international agreements and institutions poses a major impediment to global sustainable development. See UNEP, *Global Ministerial Environment Forum*, Malmo, Sweden, May 2000. A related issue is that of gaps in the existing global environmental institutional "architecture": as well articulated at UNCED in 1992, MEAs do not fully take into account all aspects of sustainable development; however, this does not imply the need to create a global environmental organization, which is unrealistic at this time. See Robert T. Stranks, *Unfinished Business: Toward a Global Environmental Organization* (Ottawa: Department of Foreign Affairs and International Trade, July 1995).

[18] More generally there is a question of adequate and long-term funding for international environmental institutions, such as UNEP. The internal capacity of international environmental institutions will strongly influence their own effectiveness and their ability to contribute to increased coherence and co-operation.

Finally, trade is also more than multilateral trade rules. A wide range of variables, such as consumer preferences, not within the scope of the WTO's mandate influence actual trade flows. For example, while UNEP does not have a mandate to address WTO trade rules and the environment, its work program on "Technology, Industry and Economics" has the objective of contributing to improving the understanding and knowledge of environmental issues related to industrial and urban development, trade and the economy, sustainable consumption patterns, increased use of natural resources, and chemicals. UNCTAD's interest is in enhancing the transfer and diffusion of technologies to developing countries. Such initiatives, while focussed on technology, have important implications for both trade and the environment. These activities, particularly their funding aspects, are not appropriate for the WTO. Clearly, there is a potential for developing synergies amongst the various specialized institutions with an interest in trade and the environment. Countries need to work collectively toward developing a work plan to encourage international institutions to maximize these synergies.

Concluding Observations

The foregoing discussion points toward the conclusion that the trade and environment policy interface is fundamentally about good governance. Trade and environmental policy share the goal of improving the quality of life. To reach this goal, trade and environmental policy must also share the goal of avoiding the use of environmental measures for trade protectionist purposes.

To inform an anxious public, and to contribute to effective and coherent public policy making, further substantive understanding of the linkages between trade and the environment is required. Such an understanding can be enhanced through a coherent agenda with interrelated work within the WTO, by the WTO in co-operation with other international institutions, and outside the WTO. Moreover, the paper suggests that the trade and environment interface needs to be considered in a broader sustainable development context. The latter is necessary not only to develop a full appreciation of the complexity of the issues, but also to better engage developing countries in order to reduce mistrust and misunderstanding.

The year 2002 will mark the 10th anniversary of the Rio Earth Summit. Canada would like to see Rio+10 address cross-cutting organizational, strategic and policy issues. At the core of these issues is the need for a clear and coherent framework of global environmental governance within which efforts to protect the global environment, whether those be domestic, bilateral or multilateral, can take place. One of the important questions the international community will need to consider over the next two years, as part of the preparations for Rio+10, is how to engage developing countries in the global sustainable development agenda, and strengthen their capacity to contribute to international efforts to address global environmental challenges. Over the coming years, a number of international institutions, including the WTO, have an important role to play in this regard.

Trade, Employment and Wages: A Review of the Literature

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Introduction

The impact of increased trade and investment liberalization on employment and wages is a matter of considerable debate. Those opposing freer trade argue that rising imports from low-wage developing countries are displacing low-skilled workers in advanced economies. Investment liberalization is seen as exacerbating this problem by enabling multinational enterprises to relocate their manufacturing operations to take advantage of low wages in these countries. These developments are seen as a primary cause of the decline in relative employment and wages of low-skilled workers and of rising income inequality and/or unemployment in many countries, including Canada, particularly in the early 1990s.

Proponents of liberalization, on the other hand, argue that trade and investment liberalization results in a reallocation of resources to areas of comparative advantage, thereby raising productivity and growth over the long term. This in turn provides the basis for improvement in employment and wages, offsetting any short-term employment losses and transitional problems for some groups of workers.

In Canada, the debate over the labour market impacts of trade have focussed more on the Canada-U.S. Free Trade Agreement (FTA) and the subsequent North American Free Trade Agreement (NAFTA) than on trade with developing countries, but the underlying anxieties appear to be similar. Indeed, the Canadian manufacturing industry suffered significant employment losses in the period following the implementation of the FTA. As Gaston and Trefler (1997) state: "Nothing has undermined the position of free-traders more than the dismal performance of Canadian manufacturing employment since the implementation of the Canada-U.S. FTA."

This paper reviews the evidence on the impact of trade on employment and wages. First, the theoretical mechanisms through which trade and foreign investment impact on labour markets are discussed. This is followed by a brief review of the main theories on the labour market impacts of international trade, an examination of the evidence regarding the impact of trade on employment creation and an examination of the impact of trade and investment with developing countries on domestic employment and wages. The paper concludes by briefly outlining some general policy issues and identifying some knowledge gaps.

Trade and Labour: Theoretical Considerations

Before examining what theory predicts about the impact of trade on labour markets, it is useful to briefly examine recent Canadian trends in trade and investments abroad.

Recent trends in Canada's international trade

Over the 1990s, Canadian exports and imports of goods and services increased significantly, roughly doubling between 1990 and 1999. As a result, the Canadian economy has become increasingly outward-oriented. The ratio of exports and imports to GDP increased from 26 percent respectively in 1990 to 43 percent and 40 percent respectively in 1999 (Industry Canada, 2000a).

Most of the growth in Canada's trade has occurred with the United States at the expense (in relative terms) of other regions (see Table 1). The U.S. share of Canadian exports increased from 74.2 percent in 1990 to 86.8 percent in 1999. Similarly, the U.S. share of Canadian imports increased from 64.5 percent to 67.3 percent between 1990 and 1999. The share of Canada's trade with other regions (exports and imports) tended to decline over this period. In general, Canada trades with other developed countries. In 1999, roughly 95 percent of Canadian exports and 90 percent of Canadian imports were exchanged with other countries of the Organization for Economic Co-operation and Development (OECD).

Table 1
Canadian Merchandise Export and Import Market Shares by Region

	Export Shares		Import Shares	
	1990	1999	1990	1999
United States	74.2	86.8	64.5	67.3
EU	8.9	4.7	12.7	9.9
Latin America	1.9	1.6	3.4	4.6
Asia-Pacific	10.9	5.2	14.0	13.3
Other	4.2	1.7	5.4	4.8
OECD	92.2	95.7	89.7	87.9

Source: Industry Canada, Trade Data Online (http://strategis.ic.gc.ca/sc_mrkti/tdst/engdoc/tr_homep.html).

Recent trends in Canadian direct investment abroad

Recent trends in Canadian direct investment abroad (CDIA) have also contributed to increasing the outward orientation of Canada's economy. Between 1988 and 1998, the stock of CDIA approximately tripled. As a result, CDIA as a share of GDP increased from 14.8 percent to 30.9 percent over that period (Industry Canada, 2000b).

Most CDIA is directed toward the United States. However, the U.S. share of total CDIA declined during the 1990s, falling from 64 percent in 1988 to 53 percent in 1998 (see Table 2). The Latin American share of CDIA increased the most, rising from 8.7 percent to 18.1 percent over that period. CDIA to the European Union and Asia-Pacific regions also increased slightly. As is the case with trade, however, the destination of most CDIA was to developed countries, with the United States and the EU accounting for around 72 percent of total outflows.

Table 2
Distribution of Canada's Stock of Direct Investment Abroad, by Region

	1988	1998
United States	64.0	52.6
European Union	17.7	19.3
Latin America	8.7	18.1
Asia-Pacific	5.4	6.1
Other	4.3	3.9

Source: Industry Canada (2000b), "Trends in Canada's Outward FDI – An Analysis of the New Database" (http://strategis.ic.gc.ca/pics/ra/ofdi_e.pdf).

Theories of international trade

There are two main theoretical approaches that describe the channels through which international trade might impact on the labour market. The first is the Hecksher-Ohlin (H-O) theory of comparative advantage, which offers predictions about the impact of trade between countries with different resource endowments that can be applied to the case of trade between developed and developing countries. The second approach is subsumed in what are called "new trade theories" that were developed to describe trade between developed countries with similar resource endowments. As seen above, most world trade today occurs between developed countries.

The H-O theory posits that comparative advantage arises from differences in relative endowments of factors of production (e.g. land, natural resources, labour and capital). Countries will therefore specialize in the production of goods that use their relatively abundant factor. Skilled labour is relatively more abundant in developed countries, while unskilled labour is relatively more abundant in developing countries. Thus, the theory predicts that, in their trade with developing countries, developed countries would export skilled-labour-intensive goods and services and import unskilled-labour-intensive goods and services. There is evidence that this prediction indeed does reflect actual patterns of trade between developed and developing countries (OECD, 1994).

According to this theory, an intensification of trade with developing countries would, therefore, tend to reduce the demand for low-skilled workers in developed countries as well as their relative wages, all other things being equal. The magnitude of the impact on relative wages would depend on their responsiveness to changes in demand. In countries where wages are flexible, such as the United States and Canada, increased trade with developing countries would tend to lead to a fall in the relative wages of low-skilled workers. In countries where wages are more rigid, such as in Europe, increased trade with developing countries would be reflected mainly in higher unemployment for low-skilled workers.

Another prediction of the H-O theory is that trade will lead to a convergence in factor prices across countries. This tendency would also be reflected in the price of traded goods.[1] Researchers looking to estimate the magnitude of the impact of trade on OECD labour markets will often look at whether the prices of goods that are subject to import competition exhibit a tendency to fall.

The so-called "new trade theories" were developed to explain the fact that most OECD trade is between countries with similar factor endowments and is characterized by intra-industry trade of similar (but differentiated) products. In developed countries, the production of manufactured goods is primarily characterized by imperfect competition where specialization leads to lower costs via economies of scale and hence improved competitiveness. In the presence of economies of scale, the enlargement of markets permits further cost reductions for the firm and there will be an incentive to export if trade barriers are reduced. One of the main predictions of the theory is that intra-industry trade will be more intense between countries with similar incomes, tastes and production structures.

According to the new trade theories, the gains from trade occur because production costs fall as the scale of output increases, which translates into lower prices. However, the theory's predictions about the impact of intra-industry trade on relative wages are ambiguous. Changes in the demand for, and hence the wages of, high- and low-skilled workers will depend on how the production of some goods falls and of others increases. The demand for unskilled workers will depend on the types of technologies used in expanding and declining firms and how the technologies themselves change in response to changes in the level of production. It is therefore possible that developed countries will export both skilled-labour-intensive and unskilled-labour-intensive products.

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[1] This is also known as the Samuelson-Stolper Theorem, which shows that, under certain conditions, trade will lead to the equalization of the prices of factors and of goods.

However, while society as a whole benefits from lower prices and higher consumption possibilities, the displacement of resources invariably creates losers. In a context where more recent waves of technological change appear to have favoured more skilled workers, the losers may well be unskilled workers.

Trade and Employment: The Canadian Experience

Studies of the impact of trade on employment in Canada focus mostly on the experience of the 1970s through to the early 1990s. During this period, the structure of employment in Canada shifted, with the share of manufacturing declining relative to services. In the 1980s, the manufacturing sector actually suffered net job losses as employment declined by about 0.5 percent per year between 1981 and 1991 (Gera and Massé, 1996). In general, manufacturing employment losses were concentrated in low-technology, labour-intensive sectors, while high-technology, skill-intensive sectors experienced employment gains (Gera and Massé, 1996; Baldwin and Rafiquzzaman, 1998).

What is the role of trade in explaining these employment patterns? Input-output analysis (I/O) conducted by Gera and Massé (1996) suggests that the importance of trade in explaining changes in the industrial structure of employment increased during the late 1980s and early 1990s. That is, trade now accounts for a larger share of employment variations relative to other factors such as domestic demand and productivity than was the case during the 1970s.

In the manufacturing sector, the study found that exports have become a dominant factor in employment growth in high-technology and skill-intensive industries, while import penetration adversely affected employment growth in low-technology, labour-intensive industries. This is consistent with international evidence which shows that trade has been associated with job losses in labour-intensive sectors such as textiles, clothing, wood and leather (OECD, 1994, 1996).

The role of trade in explaining employment changes in service industries also appears to have increased. While domestic demand remains the main determinant of employment in services, the study found that exports and imports explain a larger share of employment changes in services in more recent years, particularly in the 1980s. Exports affected employment positively in "high-knowledge" services such as business services and finance, insurance and real estate. In contrast, import penetration was associated with employment losses in "low-knowledge" services such as transportation services and food and accommodation services, particularly in the second half of the 1980s.

A central question is whether employment gains in export-oriented and related sectors compensate for employment losses in industries facing import competition. It is first worth pointing out that a large number of jobs in Canada depend on exports. Gera and Massé (1996) found that the expansion of exports accounted for around 75 percent of new jobs (1.4 million) between 1971 and 1991. A recent study by Statistics Canada (1999) estimates that in 1995 around one in five jobs in Canada was directly or indirectly related to exports.

On balance, the available evidence suggests that the net impact of trade on employment has been positive. Gera and Massé (1996) found that, despite the negative employment impact of imports, trade accounted for 23 percent (719,000) of net new jobs in Canada between 1971 and 1991. However, during the second half of the 1980s, trade had a small net negative impact on employment.

It is also worth pointing out that imports do not necessarily imply job losses. According to Cameron and Cross (1999), over one third of the rise in the share of exports to GDP has been due to the rising import content of exports, resulting from the increasing international specialization of production. In fact, import content has increased the most in industries where export growth has been the strongest. There is evidence that the growing import content of exports has led to slower growth in export-related employment than might have been expected given the growth in exports as a share of output (Dungan and Murphy, 1999). However, in the context of growing international specialization, it may no longer be appropriate to view imports, from this narrow labour market perspective, as necessarily destructive of jobs.

Employment impact of the Canada-U.S. FTA

Several recent Canadian studies of the employment impacts of trade have focussed on the impact of the Canada-U.S. FTA implemented in 1989. For example:

- Gaston and Trefler (1997) argue that the FTA was not the primary cause of most of the job losses in the Canadian manufacturing sector during the 1989-1993 period. According to the authors, FTA tariff cuts account for only 15 percent of employment losses. They find that most of the employment losses were due to the recession of the early 1990s, which they attributed to the Bank of Canada's fight against inflation, a consequence of which was high domestic interest rates and a strengthened Canadian dollar.
- Schwanen (1997) argues that the FTA did not contribute to Canada's employment problems in the early 1990s. Sectors most sensitive to the FTA do not appear to have fared worse than manufacturing as a whole. Moreover, he argues that the poor employment performance of some sectors was primarily due to factors other than the FTA – for example, import competition from non-U.S. sources (leather and electronics products), the recession

(construction materials) or long-term decline not related to trade (fish products, shipbuilding).

- Trefler (1999) finds that the FTA reduced employment in manufacturing by about 5 percent over the 1988-1996 period. Industries exposed to large tariff cuts experienced relatively large employment declines of about 15 percent over that period.

In general, the evidence suggests that the employment impact of the FTA, while largely negative in the most affected sectors, appears to have been small relative to total employment. The available evidence does not allow an assessment of whether the FTA has resulted in net employment gains or losses. Factors other than the FTA also appear to have played an important role in the evolution of employment. Restrictive macroeconomic policies, the appreciation of the Canadian dollar, and the early 1990s recession clearly make it difficult to isolate the impact of the FTA.

In sum, there is little evidence that trade in general or the FTA in particular has led to large employment losses overall. Viewed over a long period, trade appears to have contributed positively to employment growth in Canada. That said, where trade has had a negative impact on employment, it has been mostly in low-technology, labour-intensive sectors, which employ large numbers of low-skilled workers.

Trade, Employment and Wages: The Experience of Low-Skilled versus High-Skilled Workers

There is an ongoing debate over the role of trade with developing countries in explaining the decline in the relative employment prospects and wages of low-skilled workers and increased income inequality in developed countries. There is disagreement among researchers over the magnitude of the trade impact relative to that of other factors such as technological progress and institutional changes.

There are essentially two types of empirical approaches that attempt to measure the impact of trade with developing countries on the employment and wages of low-skilled workers: factor content studies and price effect studies. Factor content studies attempt to calculate the number of low-skilled workers employed in the production of a particular country's exports and the amount that would have been employed to produce that country' imports. The net impact of trade is interpreted as being the difference between the two. Price effect studies examine if the relative price of unskilled-labour-intensive goods have fallen as predicted by the factor price equalization theorem discussed above.

According to recent reviews of both factor content and price effect studies (mostly based on U.S. experience), the OECD (1996, 1997, 1998, 2000) concludes that trade is not the main driving force behind increased demand for skilled workers in OECD countries. There is evidence that trade did contribute to the declining fortunes of low-skilled workers and increased income inequality, but the effect was limited. The OECD (1998) estimates that increased trade with developing countries accounts for only about 10 to 20 percent of the changes in wages and income distribution in developed countries.

Researchers arguing that the impact of trade is small often point to the fact that industrialized countries primarily trade with each other. As shown above, around 90 percent of imports to Canada come from other OECD countries. Although trade with developing countries is increasing, it still represents a small part of total trade in manufactured goods.

There are only a few studies on the link between trade and the relative wages of low-skilled workers in Canada. These focus on the manufacturing sector only and offer somewhat conflicting evidence. Some find a positive impact of trade on the relative wages of low-skilled workers in Canada. For example, Trefler (1999) finds that the FTA increased the relative wages of production workers relative to non-production workers in manufacturing. Gu and Whewell (2000) find that imports to Canada are in fact more skilled-labour-intensive than Canadian manufacturing exports and suggest that increased trade has not hurt the wages of unskilled versus skilled workers.

In contrast, Baldwin and Rafiquzzaman (1998) find a direct link between increases in the wage premium of skilled workers and changes in trade intensity. Sectors where import competition increased the most (labour-intensive, product-differentiated and natural resources sectors) also saw the largest increases in the wage premium of non-production workers. However, these results are not directly comparable to those above, as the authors examine changes in relative wages at only a sectoral level and do not provide evidence for manufacturing as a whole.

The evidence suggests that while trade has indeed had some negative impact on the demand for low-skilled workers, the effect remains relatively small compared to other factors. While there is still disagreement among researchers, there is a growing weight of opinion that technological change favouring skilled workers is probably the dominant factor (OECD, 1996, 2000). In Canada, the evidence suggests that the increase in the demand for skilled workers is widespread across all sectors of the economy (Lavoie and Roy, 1998). This evidence suggests that the source of employment changes is systemic and is consistent with the technological change argument. There is also more direct evidence of a positive link between measures of technological change and the employment of skilled workers (see, for example, Lavoie and Therrien, 1999; Gera, Gu and Lin, 1999; Baldwin, Gray and Johnson, 1997).

In reality, growing trade and technological change are interrelated processes. For example, increased international competition may induce firms to adopt new technologies to remain competitive. Conversely, new technologies support the expansion of international trade by providing the basis for increased specialization and increased economies of scale, enabling firms to operate on world markets (OECD, 1994). Indeed, Baldwin and Rafiquzzaman (1998) find evidence that both skill-biased technological change and trade have contributed to increased wage differentials between skilled and unskilled workers in manufacturing industries.

Alternative hypotheses

Most of the literature on the impact of trade on employment and wages has focussed on the role of trade in reducing the demand for unskilled workers in industrialized countries. In a recent book, Harvard Professor Dani Rodrik (1997) suggests that trade affects not only the quantity of labour but its *elasticity* as well, which in turn has implications for real wages. He argues that globalization enables the services of large segments of the population, low-skilled workers and middle managers in particular, to be more easily substituted by the services of people in other countries. The consequence of increased instability in labour demand is greater instability in earnings and hours worked for such workers. It would also erode their bargaining power in setting the terms of employment. The author argues that this is an additional source of tension underlying the anxieties about globalization. As yet there is little evidence on the magnitudes of these effects.

A somewhat similar trade-based hypothesis is advanced by Bhagwati and Dehejia (1994) to explain increased differentials between skilled and less-skilled workers. The authors argue that increased economic integration and the rise of multinational enterprises have increased the volatility of comparative advantage – firms and industries have become more "footloose" as small shifts in costs can cause comparative advantage to shift suddenly from one country to another. Increased volatility in comparative advantage leads, in turn, to increased labour turnover. Increased labour turnover reduces the relative wages of the lesser skilled, either because they have skills that are less easily transferable than those possessed by skilled workers or because they are less likely than high-skilled individuals to invest in skill upgrading during jobless spells. Zalkilwhal (2000) finds some empirical support for the Bhagwati-Dehejia hypothesis for Canada over the early 1990s.

Earnings inequality in Canada

The international debate over the impact of trade and technology on earnings inequality, particularly in the United States, has focussed on the declining relative employment and wages of low-skilled workers. In Canada, the debate regarding the sources of increase in earnings inequality is less clear.

Unlike in other countries such as the United States and the United Kingdom, the wages of high-skilled workers relative to low-skilled workers in Canada have not increased over the past 20 years or so.

While the demand for skilled workers has increased, the supply of educated workers has also increased significantly. According to some researchers (e.g. Murphy, Riddell and Romer, 1998), the stability in the skill premium merely reflects the fact that increases in the supply of skilled workers have offset the demand effects of skill-biased technological change. A similar story could apply to the effect of trade, but the Canadian literature has tended to focus on the technological change argument.

In Canada, wage differentials have arisen primarily between older and younger workers, and there is evidence suggesting that these differentials are not related to the effects of either trade or technology (e.g. Beaudry and Green, 1999). Factors identified in the literature as contributing to increased inequality in Canada, particularly that between older and younger workers, include changes in labour market institutions such as minimum wages and unionization, changes in women's labour force participation patterns, and increased education among older workers.

There is still no consensus among researchers on the relative importance of these various factors, but explaining inequality trends in Canada is more than a matter of discriminating between the effects of trade and technology. More research is required to get at the sources of increased earnings inequality in Canada.

Foreign direct investment, employment and wages

It is often argued that the expansion of multinational enterprises (MNEs) has lowered the wages of workers in industrialized countries as they establish foreign affiliates and outsource jobs. Sometimes, the mere threat of outsourcing is seen as reducing domestic workers' bargaining power and holding their wages down. There is therefore a concern that lower wages in developing countries provide them with an unfair competitive advantage, thereby undermining employment prospects in industrialized countries.

According to recent reviews of the evidence by the OECD, the available research suggests that increased foreign investment and the outsourcing of production exert only moderate influences on labour markets in industrialized countries (OECD, 1994, 1998). Some of the main arguments advanced to support this view are as follows:

- Competitive advantage is driven by differences in unit labour costs and not necessarily by low wages. Low wages usually reflect low productivity, which generally results in there being much smaller differences in unit labour costs than those observed for wages.

- Like trade, foreign investment occurs mainly among OECD countries. As noted earlier, the United States and EU account for around 70 percent of Canada's outward direct investment flows.
- When investing outside the OECD, firms tend to invest in the richest markets, not the ones with the lowest wages. Moreover, evidence on the activities of U.S. MNEs shows that overall employment in their foreign affiliates actually fell between 1977 and 1994 (Lawrence, 1996, cited in OECD, 1998).
- The location decisions of firms are mainly determined by factors other than wages. These include proximity to suppliers and consumers, access to quality transportation and communications infrastructure, access to a skilled workforce, and a favourable legal environment for investors.

Policy Implications and Knowledge Gaps

In Canada's case, the evidence suggests that the importance of trade in explaining employment changes in both manufacturing and services sectors is increasing. There is little evidence that trade in general or the FTA in particular has led to large employment losses overall. Viewed over a long period, trade appears to have contributed positively to employment growth in Canada, particularly in high-technology, skill-intensive sectors. On the other hand, trade appears to have had a net negative impact on employment in low-technology, labour-intensive sectors, which employ relatively large numbers of low-skilled workers.

Exports are clearly an important source of jobs in the Canadian economy. With the expansion of world markets, policies that foster greater competitiveness of exports would contribute to the capacity of the Canadian economy to generate jobs. At the same time, the import content of Canadian exports has risen significantly during the 1980s and 1990s, particularly in sectors where exports have risen the most. More needs to be known about the employment effects and resulting policy implications of this development.

The evidence also indicates that trade and investment behaviour of MNEs with respect to developing countries is likely to have more negative employment and wage impacts for low-skilled workers than high-skilled workers. However, the available evidence suggests that the magnitude of these effects is likely to be small. Although there is still disagreement among researchers, the evidence appears to favour technological change over trade as the main factor explaining the increasing demand for high-skilled relative to low-skilled workers. While the literature tends to treat trade and technology as separate factors, they are in reality complementary and interrelated processes. From a policy perspective, both trade and technology interact to increase the demand for high-skilled workers relative to the low-skilled. The main challenge for policy is how best to cope with this development and to ensure that the gains from trade are distributed more evenly.

Two main policy considerations arise in this respect. The first concerns the types of social protection policies required to facilitate the transition of displaced workers from shrinking sectors or firms to expanding ones. This involves developing the proper mix of "passive" income support schemes with appropriate work incentives and more "active" measures that assist the unemployed to compete successfully for new jobs (e.g. job placement services, training programs, job subsidies). Second, in the longer term, the pressures from globalization and technological change point to the need to upgrade the skills of the population so that workers are able to take better advantage of new opportunities and to adapt more easily to changing circumstances.

Pressures from trade are likely to continue as emerging, labour-abundant economies such China and India become more integrated in the world economy (OECD, 1997). Moreover, new technologies are increasingly available to developing countries and may enable them to compete more directly with developed countries in the future.

As a result, continued monitoring of the labour market effects of trade is warranted. Further assessment of alternative hypotheses on the labour market effects of trade such as those advanced by Bhagwati and Dehejia (1994), Zalkilwhal (2000) and Rodrik (1997) also constitute avenues for further research.

Finally, while trade with developing countries appears to have had a limited impact on the Canadian labour market in the aggregate, its impact obviously varies from one industry to another. Some industries are more exposed or sensitive to trade than others. Some may have particular characteristics (e.g. type of production technology) that interact with trade, resulting in sector-specific policy challenges. As a result, industry-level analyses are required to enhance the assessment of the impact of trade and its implications for adjustment in terms of employment and wages.

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Part III

Implications for Trade Policy

The Case for a New Round: Has It Been Made?

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This paper was prepared for the 2000 National Policy Research Conference. The paper draws heavily on the results of research papers prepared for, and seminar discussions held under the aegis of, the interdepartmental Working Group on World Trade Issues constituted under the Global Challenges and Opportunities Network (GCON). The paper also draws heavily on discussions held at the Department of Foreign Affairs and International Trade over the course of 2000, which were enriched by the participation of several of the leading scholars on international trade, and on some of the new trade policy literature that emerged during the course of 2000. The views expressed in this paper are those of the author; errors of interpretation or fact are the sole responsibility of the author as well. The usual disclaimer in respect of research prepared in a personal capacity by those in the public service also obtains: the views expressed are not to be attributed to the Department of Foreign Affairs and International Trade or to the Government of Canada.

Introduction and Overview

It is now exactly a year since the failed World Trade Organization (WTO) Ministerial meeting in Seattle. The past 12 months have afforded ample opportunity for post mortems and stocktaking, debate and research, and the synthesis of new views. Where does all of this leave trade policy?

First, there remains more or less general agreement within the trade policy community on the answers to the free trader's fundamental catechism:

- Is trade necessary for growth and development? Yes.
- Is opening up to trade *sufficient* for these ends? No – sound macro-, micro- and mezzo-economic policies, proper sequencing of reforms, and good governance broadly writ are also necessary.[1]
- Is the multilateral system working? Yes.
- Are there nonetheless further gains to be had from further liberalization? Yes.
- Do these gains have to be better distributed within domestic economies and between North and South? Yes.
- Do the developing countries need help to access these gains? Yes.
- Are reforms needed to the multilateral institutions and the WTO in particular to achieve these goals? Yes.

All this being said, the way ahead is not entirely clear. There is disagreement as to how far and how fast to go, and some would even argue that globalization has gone too far already. To some extent, there are even questions as to which direction to take as there is currency to the view that some of the new directions taken in the Uruguay Round represent missteps. Moreover, some believe that regional agreements offer greater opportunities than the multilateral route.[2] Finally, what might be termed the mainstream view is held with less conviction than it was pre-Seattle. This is significant in and of itself because, unlike the situation following previous failed Ministerials, which foundered on questions of content and pace, the Seattle Ministerial collapsed on questions of the desirability, as well as content and pace, of future liberalization.[3] In short, the case for a new round has implicitly been called into question.

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[1] This is often referred to as the "Washington Consensus," which is not really a consensus, at least outside the circle of governments.

[2] The general view of preferential regional trading arrangements has been that their trade-creating and other beneficial aspects dominate the trade diversion to which they give rise. Indeed, a recent study suggests that the regional route to free trade might actually lead to larger welfare gains than the multilateral route because the regional pact might offer greater incentives for firms to incur the large fixed costs in terms of distribution and marketing required to enter the export market in the first place. See Caroline Freund, "Different Paths to Free Trade: The Gains from Regionalism," *The Quarterly Journal of Economics*, Vol. CXV, No. 4, November 2000. At the same time, criticisms have been levelled at regional initiatives because of the proliferation of rules of origin, which generate not insignificant costs of compliance; moreover, in some cases, such as the United States, Africa and

This paper addresses this issue. First, it considers the evidence for further gains from trade. Since these gains appear to depend to an important extent on the integration of developing countries into the trading system, the paper addresses the likelihood of this being achieved.

Gains from Further Liberalization

An important preliminary question is: What is at stake in economic terms from further liberalization? On the face of it, despite the enormous growth in trade and investment over the past half century,[4] the evidence of a very strong "home bias" in

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Caribbean Bill, it has been argued that the distortions may well outweigh the trade creation.

[3] This argument is advanced by W.A. Dymond and M.M. Hart, "Post-Modern Trade Policy: Reflections on the Challenges to Multilateral Trade Negotiations after Seattle," *Journal of World Trade* 34(3): 21-38, 2000.

[4] Merchandise exports are currently at about 25 percent of global GDP, with cross-border trade in services at about 7 percent. Meanwhile, the value of sales by foreign affiliates of multinational companies now is roughly equal to cross-border trade in the case of merchandise and is well over one and one half times the value of cross-border trade in services. Adding these together, total exports of goods and services, defined in this broad manner, would appear to be in the order of two thirds of global GDP, with imports, of course, accounting for a similar share. For a discussion, see J.M. Curtis, "Trade and Civil Society: Toward Greater Transparency in the Policy Process," in J.M. Curtis (ed.), *Trade Policy Research 2001*, Department of Foreign Affairs and International Trade, 2001. The degree of openness varies widely by country, with the world's largest and arguably most highly developed economies – the United States and Japan – being among the least "open" (as measured by the sum of cross-border imports and exports divided

trade and investment suggests that there remains considerable scope for additional expansion of trade.[5] Jeff Frankel recently summarized the current understanding, based on so-called "gravity models" of international trade, of the trade-inhibiting effects of various factors as follows:[6]

- *Borders:* two firms located on opposite sides of a national border trade two thirds less than if they were located in the same country.[7]

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by GDP), and small highly developed economies such as the Netherlands and Canada being among the most open. What is of particular interest is that, measured by cross-border trade as a percentage of GDP alone, the United States is not much more "open" than it was a century earlier and Japan is actually less "open" on that basis than it was a hundred years earlier. At the same time, the United States is generally considered to amongst the most "open" economies in terms of ease of entry, while Japan is thought to be amongst the least open in this sense. These observations emphasize that caution is warranted in drawing conclusions about the linkage between trade policy and measured openness or the scope to expand trade (since expansion of the internal market and/or decline in price differentials internationally may reduce the incentive to seek markets beyond national borders).

[5] For a discussion of home bias and related empirical puzzles in international trade and investment, see M. Obstfeld and K. Rogoff, "The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?" *NBER Macroeconomics Annual 2000* (forthcoming).

[6] J. Frankel, "Assessing the Efficiency Gain from Further Liberalization," paper delivered at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Harvard University (June 1-2, 2000). This paper is available online (http://www.ksg.harvard.edu/cbg/trade/frankel.htm).

[7] This estimate of the size of the border effect is not directly comparable to others cited in some of the literature since it is net of common currency and other effects. John Helliwell estimates the border effect for Canada-U.S. at 10-12 for merchandise trade and for services at over 30. He also cites estimates for the European Union at between 6 and 19 and for other OECD countries at 10 or more. For developing countries, the border effects are much larger. See J.F. Helliwell, *Globalization: Myths, Fact and Consequences*, Benefactors Lecture, 2000, C.D. Howe Institute, October 2000.

- *Distance:* if two countries are not adjacent, trade falls by half, with a further 1 percent decline in trade for each 1 percent increase in distance between them.[8]
- *Currencies:* use of different currencies (even if fixed exchange rates are used) reduces trade by two thirds, with a further 13 percent reduction due to exchange rate variability.[9]
- *Culture:* if two countries speak different languages, trade falls by half.
- *Trade rules:* if two countries do not belong to a free trade area, trade falls by two thirds – and even further if the tariff and non-tariff barriers are at the heights typically found in developing countries.

Even ignoring completely the pure effects of distance and formal trade barriers, these various factors would reduce, for most country pairs, the likelihood of an international transaction taking place between two firms to less than 5 percent of that of a domestic transaction. Add in distance and trade barriers, and the likelihood falls to something on the order of 1 percent.

Most of these factors cannot be addressed through the WTO or multilateral negotiations. Moreover, those that can account for only a tiny fraction of the overall extent of inhibition of trade.[10] Nonetheless, these gains are not to be sneered at.

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[8] Helliwell puts the distance elasticity at 1.5. See J.F. Helliwell, ibid.

[9] A recent study by Andrew Rose found the smallest point estimate of the expansion of trade within a common currency zone to be 285 percent, and most were larger. See A. Rose, "Common Currency Areas in Practice," paper presented at the Bank of Canada seminar *Revisitng the Case for Flexible Exchange Rates*, November 1, 2000. The estimate cited by Frankel is thus on the conservative side. There are important questions surrounding Rose's findings (e.g. whether the direction of causality runs from strong trade linkage to common currencies and whether the results can be generalized from a rather unrepresentative sample of countries); however, for the purposes here the point is moot since anything not explained by common currencies would have to be added back into the general and otherwise unexplained "border" effect.

[10] Helliwell argues that the explanation for the very high border effects rests on the extent of networks of association and trust. These are developed

Several recent econometric estimates suggest trade expansion on the order of 20 percent could be leveraged by a new round,[11] with significant gains implied for real GDP: static efficiency gains would amount to between 1 to 1.5 percent of global income[12] with additional dynamic gains driven by the expansion of trade on the order of 6.5 percent,[13] for a total of perhaps 7.5 to 8 percent additional global GDP – in the ballpark of US$2.25

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through a multitude of means but importantly include things like casual contact, which happens frequently only in a restricted locale. This argument recalls, of course, Robert Putnam's thesis concerning the importance of informal institutions such as bowling leagues and choirs – social capital in general terms – to good economic performance. See R. Putnam, "Bowling Alone: America's Declining Social Capital," *Journal of Democracy* 6:1, January 1995, 65-78.

[11] Based on results obtained by T. Hertel, "Potential Gains from Reducing Trade Barriers in Manufacturing, Services and Agriculture," 24th Annual Economic Policy Conference, Federal Reserve Bank of St. Louis, Oct. 21-22, 1999.

[12] This range is suggested by the following estimates: Hertel (1999): US$350 billion, with the major contributions obtaining from liberalization of agriculture, manufacturing and services, in that order. Nagarajan (1999): US$400 billion, or 1.4 percent of global income, with the gains obtaining from trade facilitation and across-the-board tariff reduction; plus an additional US$85 billion from an agreement on competition (interestingly, Nagarajan models trade facilitation as a reduction in transport costs, a technique pioneered by Japan in its 1997 Asia-Pacific Economic Cooperation Economic Committee study on the gains from APEC's Trade and Investment Liberalization and Facilitation program). Dee and Hanslow (2000): US$260 billion, of which $130 billion comes from services, $80 billion from manufactures and only $50 billion from agriculture. Dee and Hanslow factor in foreign direct investment effects in their study. See P. Dee and K. Hanslow, "Multilateral Liberalisation of Services Trade," Productivity Commission Staff Research Paper, Ausinfo, Canberra (2000); T. Hertel, "Potential Gains from Reducing Trade Barriers in Manufacturing, Services and Agriculture," op. cit.; N. Nagarajan, "The Millennium Round: An Economic Appraisal," Economic Papers No. 139, European Commission, DG for Economic and Financial Affairs, November 1999.

[13] This is based on the commonly used rule of thumb that a one percentage point gain in trade leverages one third of a percentage point growth in income.

to $2.4 trillion, or two good years of global growth at the present level of global income, spread over several decades.[14]

While the gains that can be obtained through a multilateral round are considerable in gross terms, several considerations suggest that the net gains are likely quite substantially smaller.

First, these gains are not net of frictional adjustment costs. Insofar as liberalization changes the economic parameters under which existing investment was put in place, it leads to early write-down of investment, a dead-weight loss that needs to be subtracted from the efficiency gains made elsewhere.

Second, the gains are not net of risks of destabilization. For example, since potential income is depressed during downturns by the decrease in investment during the downturn, an episode of balance of payments instability as a country adjusts to new competitive pressures and consumption patterns under freer trade could easily wipe out gains from liberalized trade for some years. While the risks of instability associated with trade are more likely to come from disruption of existing trade than exposure to new trade, one cannot entirely discount the risk of opening up, especially to previously highly sheltered economies such as transition economies. At the same time, other policies associated with openness to trade (or put in place to facilitate trade) can lead to instability. Korea's experience with capital account liberalization, which was required for it to become part of the Organization for Economic Co-operation and Development (OECD), and Mexico's commitment to a strong exchange rate as an external anchor for a policy package centred on trade liberalization are cases in point.[15]

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[14] By comparison, Frankel uses Hertel's $350 billion estimate for the static efficiency gains from a new round and then, based on the 20 percent expansion of trade in Hertel's model, estimates a further 2 percent increase in global income from the dynamic gains realized over 30 years and an 8 percent increase in the "truly long run." Accordingly, the gains (in terms of permanent income levels) from a new round could be quantified at about 3.2 percent of current global income, or close to US$1 trillion, to be realized fully only in 30 years, and nearly triple that in the "truly long run." See J. Frankel, "Assessing the Efficiency Gain from Further Liberalization," op. cit.

Third, the effects of trade expansion on the environment are not taken into account – which, it should be noted, is not through disregard but because the accounting is extremely complex and quantification well nigh impossible.[16]

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[15] As a practical matter, adjustment can take years and downturns can be very deep. For example, for much of the 1990s it was hard to distinguish Russia's structural adjustment from an economic death spiral. However, even if countries have rapid recoveries, which was the case in both Mexico and Korea, both of which had V-shaped recoveries in real terms, exchange rates may remain well below pre-crisis levels (as has been true for both Mexico and Korea), reducing their gains from liberalization measured in U.S.-dollar terms, which arguably is the relevant measure since what matters in trade is what a country can afford to buy on the international market. It could be argued that such risks are already taken into account in the estimates of gains from trade obtained using econometric models in that parameter estimates of the expansion of trade and incomes leveraged by trade liberalization represent averages that summarize a wide range of experiences of individual countries in varying historical circumstances. The gains from future liberalization should similarly be interpreted as averages that would reflect some very positive experiences, some average responses, and some isolated failures due to macroeconomic destabilization that might be due to liberalization. By the same token, it might be argued that these risks are higher for relatively isolated developing countries that are latecomers to an already highly developed and competitive trading system; accordingly, the historical experience of the countries that currently account for the bulk of trade and whose histories therefore dominate parameter estimates might tend to actually understate the true risk.

[16] While this issue is addressed later in the paper, a few words are nonetheless in order here as the context is somewhat different. For one thing, there is a time dimension to these effects in the form of an "environmental Kuznets curve," which links longer-term environmental improvements to growth after an initial stage where economic activity increases pollution, greenhouse gases and so forth.

There are also various pluses and minuses: trade agreements can limit environmentally damaging subsidies to agriculture, forestry and coal but also intensify pressures on the global commons. In addressing this latter issue, Frankel notes that "It is difficult to imagine…that trade is anything but bad for the survival of tropical hardwood forests." See J. Frankel, "Assessing the Efficiency Gain from Further Liberalization," op. cit.

Fourth, applying discount rates to reflect the time value of money substantially reduces the gains 20 or 30 years hence and makes the gains that are only achievable in the truly long run of little practical consequence in decisions taken today. Not only are these benefits too far off to figure practically in political economy calculations, but they are based on the assumption of no change in the underlying economic structures and relationships, which is almost certainly false.

Fifth, for public policy the relevant question is how best to deploy scarce resources – whether to advance trade negotiations or advance other policy goals – which is a question of *relative* legitimacy.[17] Taking into account the heavy lifting required to expand the trade share of GDP through trade negotiations, the fact that technology is the main driver of growth and development, with trade but a supplementary factor,[18] and the limited resources in the jurisdictions that stand to gain most from trade, the opportunity costs of pursuing a multilateral round are significant and need to be reflected in the cost-benefit analysis.

Sixth, the case has been made, by John Helliwell, that the relationship between income gains and trade expansion is non-linear – income gains from trade expansion face eventually diminishing returns. In other words, a country going from 0 to 10 percent in terms of trade share in GDP would benefit much more from trade than a country like Canada going from 85 to 95 percent. Insofar as the major part of the gains do in fact obtain at the earlier phases of opening up, most of the trade gains from a new round would have to be generated in the developing countries to validate the estimate of income generated thereby.

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[17] This observation was made by Pierre Jacquet of the Institut Français des Relations Internationales at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Harvard University (June 1-2, 2000).

[18] See, for example, arguments to this effect in J. Sachs, "A New Framework for Globalization," paper delivered at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Harvard University (June 1-2, 2000).

At the end of the day, a convincing case for the gains from further liberalization remains to be made. The empirical evidence suggests that large gains could potentially be realized in gross terms; however, there are questions about the assumptions on which these estimates are based. Moreover, public policy should be based on an estimate of the gains expressed in net present value terms with account taken of opportunity costs. This accounting remains to be done, but the expectation would be for a much reduced figure: (a) the various costs and risks associated with liberalization (adjustment costs, risk of macroeconomic instability and collateral environmental damage) tend to be front-end loaded, while the benefits are spread over several decades, with the more distant benefits subject to deep discounting in present value terms; and (b) given that trade ranks clearly second to technology as a driver of growth, the use of scarce public resources (particularly in the developing countries) for trade negotiations raises potentially significant opportunity costs. In short, the intellectual basis for a new multilateral round remains in question.

Trade and Development

If the bulk of the estimated gains from further trade liberalization are to come from bringing marginalized developing countries more fully into the multilateral trade system, what can be said about the likelihood that these gains will actually be realized? This involves several related questions: Will the developing countries engage in a new round? Will they be able to take advantage of the market opening thereby achieved to become more fully integrated into the international trading system? Will the additional trade in fact lead to growth and development? These questions are taken up in turn.

Will the developing countries engage in a new round?

This issue has been directly addressed by Jagdish Bhagwati.[19] His main thesis might be summarized as follows:

1. The uneven distribution of benefits from the Uruguay Round needs rebalancing through improved market access in key traditional areas of developing-country interest.
2. At the same time, developing countries need to genuinely buy into liberalization, as there is no "free lunch" in a system driven by the exchange of benefits – nothing offered, nothing gained.
3. Most of the "trade and..." issues (in his terms, the "trade-unrelated" issues) need to be kept on the back burner (e.g. competition policy) or clearly hived off for treatment elsewhere (e.g. labour); however, developing countries need to engage on the trade and environment issue.[20]
4. Go easy on the tempo; allow time for full implementation and adaptation to the changes engendered by the Uruguay Round.
5. On institutional and governance issues, there are three points of interest:
    - The current asymmetry between developed and developing countries in terms of power and influence in negotiations requires institutional reforms (including the "green room" process).

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[19] See J. Bhagwati, "What It Will Take to Get Developing Countries into a New Round of Multilateral Trade Negotiations," in J.M. Curtis (ed.), *Trade Policy Research 2001*, op. cit.

[20] Interestingly, another eminent trade policy commentator, Gary Hufbauer, argues that *both* labour and the environment are poison pills for the objective of getting developing countries into a new round. See G. Hufbauer, "Trade and Coherence: Where the Major Gains Lie," in J.M. Curtis (ed.), *Trade Policy Research 2001*, op. cit.

- The positions of civil society organizations (CSOs) are threatening to developing countries, and bounds on CSO influence accordingly need to be set.
- Cross-conditionality cannot be allowed either formally or through the back door as part of the "coherence" agenda being pursued by the international agencies.

Comparing the current state of play to the position laid out above, the following observations can be made. First, there has been little if any movement on the central bargaining issues between the developed and developing countries, namely agriculture and textiles.[21]

Second, the emerging evidence on growth in trade since Marrakech, which has been disproportionately in favour of the developed countries, can only serve to reinforce the view of many developing countries that they were "short-changed" in the Uruguay Round.[22]

Third, there remains a clear and deep conflict between the developed and developing country positions on the nature of a new round. The developed countries (read the United States and European Union) want to broaden the scope of trade rules. A year after Seattle, when this divide was thrown into sharp relief, it has, if anything, gotten wider as the United States has in its free trade agreement with Jordan and rhetorically staked out the position that it intends to introduce labour and environmental standards into any future trade agreement.

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[21] The recent survey of the trade scene by *The Economist* struck a relatively pessimistic tone on these issues. With regard to agricultural subsidies, it had this to say: "The WTO is determined to eliminate export subsidies throughout its membership, but try telling that to the House of Representatives – or to the French government. Frustration with rich countries' intransigence reaches from grass-roots protesters in Seattle and Prague all the way to the top; even [WTO Director-General] Mr. Moore bemoans the snail's pace at which America and Europe have implemented reforms to their markets for agricultural products and textiles. 'Sometimes I feel like the joining the kids outside' he says. 'When they say the system's unfair, they're not always wrong.'" See "The Trade Agenda," *The Economist*, November 11, 2000, p. 85.

[22] See *The Economist*, ibid., pp. 83-84.

Fourth, the conventional wisdom emerging from the Asian Crisis on the need for appropriate "sequencing" of reforms supports if anything a more cautious approach rather than putting wind in the sails of reformers bent on liberalization.

Finally, while the institutional governance issues seem to admit the possibility of compromise in the form of trade-offs amongst various conflicting interests, there is no obvious answer to the question of how such a compromise could be brokered. The WTO lacks an executive council that could put its weight behind a proposal; and the very fact of a divided term for the Director-General indicates that neither current Director-General Mike Moore nor his successor-in-waiting, Thailand's Supachai Panitchpakdi, had sufficient broad-based support within both the developed and developing country blocs to give him a strong personal hand as a deal maker.

The above observations provide no grounds for optimism that developing countries will join a new round any time soon. This conclusion is actually reinforced if one examines carefully one of the main arguments raised in rebuttal to this conclusion: since accession to the WTO is more or less equivalent to a belated buy-in to the Uruguay Round, how can one explain the fact that so many developing countries outside the WTO are lined up to get in?

There is something to this point in terms of tempering criticisms of the *lack* of Uruguay Round benefits for developing countries; however, it does not necessarily temper criticisms based on an *imbalance* of benefits, nor does it say anything in particular concerning the likely attitude of developing countries toward *further* liberalization once they have achieved membership. Asymmetry in bargaining power is real in the global trading system; the question for smaller members is whether it is better to deal with the asymmetry up front, in an accession negotiation, versus potentially in the heat of a live trade dispute with one of the major economies.[23] A risk evaluation could well lead to a rational decision to join the WTO as soon as possible even if the immediate benefits are small (or even negative). Once inside, however, with the insurance against unilateral trade actions safely in hand (i.e. having neutralized the asymmetry of power in the *application* of trade rules), there may be no further incentives for liberalization – which involves facing yet again the asymmetry of power at the negotiating phase. Moreover, given the fact that the WTO moves on the basis of consensus, membership gives even small countries in effect a veto over forward movement that is not in their interest. This would suggest that the Uruguay Round was not such a bad deal for developing countries while at the same time pointing to a potentially serious miscalculation on the part of any who may believe that getting developing countries into the multilateral system was a prelude to deeper liberalization.[24]

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[23] In this regard, consider Sylvia Ostry's description of the U.S. threat of trade sanctions in pressuring developing countries to accept a deal on intellectual property rights. As she explains, "a new Special 301 of the 1988 Trade and Competitiveness Act was targeted at developing countries with inadequate intellectual property standards and enforcement procedures. As the Uruguay Round negotiations proceeded, the message in Brasilia and new Delhi [the leaders of a group of developing countries resisting the inclusion of the "new trade policy issues" in the round] became clearer: given a choice between American sanctions or a negotiated multilateral arrangement an agreement on TRIPS began to look better." See S. Ostry, "The Uruguay Round North-South Grand Bargain: Implications for Future Negotiations," paper delivered at the conference *The Political Economy of International Trade Law*, University of Minnesota, September 2000.

[24] Moreover, it suggests that, absent willingness on the part of the United States and European Union to underwrite multilateral liberalization by eschewing to exercise their clout in negotiations, the only way to move forward on trade policy in the future might be through legal activism on the part of the dispute settlement body, an issue that will be addressed later.

Can developing countries take advantage of liberalization?

This issue is taken up by CIDA's Kerry Max.[25] Reflecting the broad consensus on the role of trade in development, Max makes several key assumptions concerning this relationship:

1. Trade liberalization can foster economic growth.
2. Economic growth is essential for poverty reduction.
3. Economic growth, though essential, is insufficient for poverty reduction, with other key needs being threefold:
    - the technical and legal implementation capacity to address WTO rights and obligations;
    - private sector development; and
    - an enabling environment in the form of governance, infrastructure and policies which are essential to the ability of both domestic and international firms to translate opportunities from trade into viable economic activities.[26]

Max then draws the connection between trade-led growth and poverty reduction, noting that this too depends on private sector development and an appropriate enabling environment.[27]

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[25] See K.D. Max, "Addressing Trade-Related Development Needs: Options for the Donor Community," in J.M. Curtis (ed.), *Trade Policy Research 2001*, op. cit.

[26] These assumptions closely parallel the so-called "Washington Consensus" view that there is a connection between openness and the dynamism of an economy, but a coherent policy framework (market-oriented domestic policies and good governance, including enforcement of contracts, protection of property rights, etc.) and some basic conditions (macroeconomic stability) are required in addition to having an open trade and investment regime, to ensure eventual convergence with OECD-level incomes. Since the Washington Consensus is applied loosely both to marginalized countries (as a prescription for exiting that condition) and to open but poor countries (as a way to take advantage of trade), it is not so much a causal theory about the role of trade or other factors in development as a general observation concerning the characteristics of successful countries.

[27] Recognizing that growth does not necessarily benefit all the poor (and indeed in some cases some of the poor may wind up poorer still – even in the long run), Max also identifies a third category of poverty reduction-targeted

Based on these assumptions, Max then considers how best the international community can support developing countries in their development ambitions and recommends a basic division of labour, with the WTO addressing the delivery of all WTO membership-specific needs (i.e. substantial trade-related technical assistance), and the donor community (including the international agencies) addressing the remaining categories of private sector development, enabling environment and poverty-targeted interventions.

What is most important in this analysis is that it identifies the need for a very substantial *increase* in support in both respects if developing countries are to be able to take advantage of liberalization.

It is well beyond the scope of this survey to consider the adequacy of the international development assistance in general or even of the trade-related component alone. Suffice it to note that there is a question of scale to be addressed. A substantial increase in support cannot be mobilized quickly, even if the political will were there and the resources were available. And the decision to commit resources has not yet been made, at least in an order of magnitude that would be clearly seen as making the difference.[28]

There is also a more fundamental question of whether getting the effective trade and supporting policies in place is in fact the answer to getting the marginalized developing countries firmly established in the trading system. A recent careful analysis of the literature by Francisco Rodriguez and

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interventions to address the unmet basic needs of those marginalized from economic activity or unable to meet their needs based on current economic participation. See K.D. Max, op. cit.

[28] The World Trade Organization has a total of only 29 staff in its Development and Technical Co-operation Divisions combined. World Trade Organization, *Annual Report 2000,* p. 104. The WTO budget is generally considered totally inadequate to the task, and the Integrated Framework for Trade-Related Technical Assistance to Least-Developed Countries, which was supposed to compensate for lack of WTO resources, has been ineffective. Max also comments on the past failures by developed countries to deliver promised technical assistance.

Dani Rodrik concludes that there is no evidence that an open orientation of trade *policy* reliably leads to growth. They argue that previous studies that had found such a relationship involved mis-specified equations in which trade openness served as a proxy for other variables (such as geography). When these other variables are included (e.g. distance from the equator), the significance of the trade openness variable vanishes. While they caution that this is not to argue that being closed to trade is a good idea, they do emphasize that there is no basis for strong conclusions about the ability to expand the trade of isolated countries by reducing policy-induced trade barriers.[29]

These observations point to two general conclusions. First, assistance in implementing trade and supporting economic policies may have little impact in the currently marginalized countries. Second, the analytical results need to be revisited to determine whether or not the trade expansion estimated to obtain from a new round of trade liberalization is overstated.[30]

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[29] See R. Rodriguez and D. Rodrik, *Trade Policy and Economic Growth: A Skeptic's Guide to the Cross-National Evidence,* May 2000 (http://ksghome.harvard.edu/~.drodrik.academic.ksg/papers.html). A similar conclusion is reached by Dan Ben-David, who notes: "it is far from obvious (at least to this author) that the impact of trade liberalisation found on incomes in the middle and high income countries could also be found in the poorest countries in the world." Dan Ben-David, "Trade, Income Disparity and Poverty," World Trade Organization, Special Studies 5, p. 39.

[30] General equilibrium models estimate the trade expansion from liberalization based on differences in factor intensities and prices in the various economic jurisdictions. Apart from transportation cost margins, they make no formal distinction between the potential for gains from trade between countries based on geographic separation or cultural and linguistic differences (although these factors are captured to some extent in the initial conditions as to the intensity of trade between two given countries built into the data set; these silently proxy the gravity effects in that, if bilateral trade is minimal, then changes in factor prices, etc., result in quantitatively insignificant effects – I am indebted to Konstantin Loukine for this point). This issue appears to be related to the question of the "missing trade" (which refers to trade "missing" compared to predictions of standard Heckscher-Ohlin trade theory), as discussed in D. Trefler, "The Case of the Missing Trade and Other Mysteries," *American Economic Review* 85 (5): 1029-1046.

Will the additional trade in fact lead to growth and development?

Finally, there is the question of whether currently marginalized developing countries could leverage expanded trade into development, even if they were able to expand their trade substantially.[31] This is important in view of the diminishing returns argument discussed earlier, which suggests that the income gains from further trade expansion on the part of the developed countries would be comparatively modest.

There is a presumption that the answer to this question is "yes," given the overall strong positive correlation between trade and growth and between economic growth and increases in income of the poorest.[32] Moreover, it can be observed that the only countries that have "taken off" in a development sense have been trade-oriented; conversely, no country that has chosen an isolationist or self-sufficiency policy has proved successful in this sense.[33]

Generally speaking, the decline in trade with distance is thought to exceed by far what could be accounted for by transportation costs alone.

[31] Note: this is a somewhat different question from what it takes to avoid marginalization – countries that are already quite open are by definition trading and not "marginalized" in that sense.

[32] Gary Hufbauer makes this point. Hufbauer also notes that, unlike the case of trade and growth, the linkage between FDI and growth is equivocal. This is somewhat curious since the causal relationship between capital accumulation and technology and growth is actually empirically better established than is the relationship between trade and growth. See G. Hufbauer, op. cit.

[33] Dani Rodrik has argued that this may not be the fault of the import replacement policies adopted by countries that have gone this route but accompanying poor macroeconomic or financial policies. While plausible, this argument is not powerful as it calls for a major selection bias (i.e. only poorly managed countries choose import replacement) and thus plays into the hands of the counter argument advanced by some that openness to trade effectively constrains bad policies and/or outcomes (e.g. through external

However, there are also countries that have not developed nearly as well as might be expected, given their degree of openness, and others that have done much better than their degree of openness would imply. This calls into question whether the observed correlation involves causation flowing from trade to growth (versus, say, from growth stimulated by third factors to trade).[34]

There are other troubling facts from an analytical perspective. Some work by Andrew Rose shows that common currencies result in at least a threefold increase in trade, significant specialization among the trading partners and also improved inflation performance. Strikingly, while many of the countries in the sample were rich, many were also poor. What this indicates is that even if there is trade and international specialization of production, there is not necessarily development.

Jeff Sachs offers an explanation for these anomalies based on the influence of geography on trade and economic performance. He holds that countries can be sorted roughly into three categories:

- a "technological first world of innovators," countries that produced at least 10 U.S. patents per million citizens in 1997;
- a second world of "technological adopters" (identified as countries that attract significant amounts of foreign direct investment in high-tech sectors and have at least some exports to first-world markets in high-tech

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commitments to market-friendly policies in order to attract investment and disciplines of international competition on domestic industries).

[34] Alan Winters has this to say on the subject of causation in the relationship between trade and growth and foreign direct investment and growth: "In both cases the problem is one of causation: efficiency and exports are linked because efficient firms export, FDI and efficiency because investors choose efficient firms and sectors." See L. Alan Winters, "Trade and Poverty: Is There a Connection?" World Trade Organization, Special Studies 5.

sectors), which tend to be clustered around the technological innovators; and

- the rest of the world, which is described as "technologically stagnant" and which tends to be geographically more distant from the technological innovators. These areas include southern Mexico and pockets of tropical Central America, the Andean countries, most of tropical Brazil, tropical sub-Saharan Africa, most of the former Soviet Union aside from the areas nearest to European and Asian markets, and landlocked parts of Asia such as the Ganges Valley states of India, landlocked Laos and Cambodia, and the far-interior regions of China.[35]

If, as is suggested by the conventional wisdom, good governance and sound economic policies determine growth and development, why should the technology content of exports and FDI and regional location be so significant? Sachs suggests that the root cause of underdevelopment is actually collapsing social structures due to disease;[36] and/or reliance on primary commodities, which are continuously being "innovated against" and hence face a long-term decline in terms of trade that makes them a very weak basis for development. Indeed, insofar as liberalization of agriculture and textiles would tend to reinforce specialization in commodities, it could even be harmful to the long-term development interests of these countries.

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[35] See J.D. Sachs, "A New Framework for Globalization," paper delivered at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Harvard University (June 1-2, 2000).

[36] This is particularly the problem for sub-Saharan Africa, which is ravaged by AIDS and other diseases incubated in the tropics. While the spread of AIDS has prompted massive investment in medical research in the industrialized countries, tropical diseases have generally not received much attention, as there is no profit prospect for Western pharmaceutical firms.

Where does the trade and development issue then stand?

With the trade and development debate up in the air, it is worth recalling past shifts in intellectual fashion on this point. In a recent article, Joe Francois draws attention to Harry Johnson's 1977 review of the state of thinking on trade and development. Francois notes that Johnson saw intellectual cycles moving between rejection and embrace of the world trading system "...with a strong bias toward the former. In looking toward the future, Johnson saw development economists placing renewed emphasis on commodity price stabilisation and monopoly trading schemes along the lines of OPEC." Francois goes on to note that things worked out very differently as "Outward oriented policies emerged as a consensus policy in the 1980s."[37]

Such shifts in conventional wisdom reflect the presence of significant "outliers" in the data. East Asian economies such as Korea and Taiwan were the outliers in the late 1970s that forced a change in the conventional wisdom of that age. There are other outliers today that call into question today's conventional wisdom, which is based largely on East Asia's experience: "On the positive side, the South East Asian economies, together with Mauritius and Chile, are good deviants. At the same time, the bad deviants include Zambia, Gabon, and Haiti."[38]

Accordingly, the mere presence of doubt regarding the linkages between trade and growth and development does not remove the very strong presumption in favour of trade. This judgement is reinforced by the evidence reported by John Helliwell that border effects are higher for R&D spillovers than for trade, and that distance matters as well.[39] If technology is the key to development, then trade may be the best source of a supplementary boost to developing countries' own efforts to develop an indigenous knowledge-generating culture.

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[37] See Joseph F. Francois, *The International Economy and Economic Development* (Francois' website, 2000).

[38] See Joseph F. Francois, ibid., p. 7.

[39] See Helliwell, op. cit., p. 35.

However, the weight of the overall evidence does caution against overselling trade as a reliable route to development. It also cautions against counting the global gains from trade as being in the bank, if those gains depend heavily on countries that are at present marginalized, without a better understanding of why they are marginalized.

Some Tentative Conclusions

The discussion above suggests that a robust case for a new round of multilateral negotiations has not yet been firmly established on analytical grounds.

- While there is still considerable untapped potential to expand trade, a number of important questions have been raised as to whether, and under what conditions, this would translate into income and welfare gains sufficient to warrant the commitment of scarce policy resources at this time.
- Moreover, insofar as the income and welfare gains from a new round would depend heavily on the integration of currently marginalized developing countries into the trade system, the discussion of "trade and development" suggests that there are simply no grounds for optimism that these gains could be realized except in the longer term and subject to considerable improvement of so-called "enabling conditions."

However, this does not necessarily leave the trade system in bad shape, or its policy making necessarily in hiatus – quite the contrary. Accession of China, Taiwan and the states of the former Soviet Union alone would generate benefits of the same order of magnitude as a new round, and with fewer of the caveats that attach to getting developing countries in general into the trading system. The development of case law by the Dispute Settlement Body is pushing the envelope both on implementation of commitments and the refinement of WTO law itself. And incremental changes to the institutional framework are well suited to a Ministerial meeting process. At the same time, this affords a window of opportunity to develop the intellectual basis for further liberalization and for the direction to take in further developing the architecture of the multilateral system, and dealing with the WTO's governance issues.

The "Trade and..." Agenda: Are We at a Crossroads?

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This paper was prepared for the National Policy Research Conference, Ottawa, November 30-December 1 2000. It attempts to provide a "horizontal" analysis of a number of trade-related issues, drawing on the results of research conducted under the aegis of the GCON Working Group on World Trade Issues and on some of the new trade policy literature that emerged during the course of 2000. The views expressed in this paper are those of the author; errors of interpretation or fact are the sole responsibility of the author as well. The usual disclaimer in respect of research prepared in a personal capacity by those in the public service also obtains: the views expressed are not to be attributed to the Department of Foreign Affairs and International Trade or to the Government of Canada.

Introduction and Overview

Disagreement over whether to develop additional multilateral instruments dealing with trade-related issues contributed to the failure to launch a new round of multilateral negotiations at the World Trade Organization (WTO) Ministerial meeting in Seattle. This disagreement persists: the United States and the European Union continue to insist on broadening the WTO agenda to include new issues, while developing countries express concern over this direction. Moreover, the epistemic trade policy community is also divided on the merits of introducing new instruments to deal with trade-related issues in the body of multilateral trade rules; there is some currency to the view that several of the new directions taken in the Uruguay Round were not well advised and that it would be better to backtrack rather than to proceed further down that path. Accordingly, the multilateral system appears very much to be at a crossroads.

This paper takes a "horizontal" look at a number of trade-related issues to see if some general principles can be identified that could provide some guidance as to the way ahead. To set up this discussion, the paper first considers trade linkages from a "first principles" perspective and briefly reviews some of the relevant history of the evolution of the multilateral system. The conclusions that emerge from this survey are as follows:

First, the application of trade rules has constrained the design of domestic policies but not the substantive intent of domestic policies. By the same token, this makes trade rules an ineffective means to get at policy objectives that are broader than trade transactions, particularly in an extraterritorial way in foreign jurisdictions.

Second, the capacity to manage risk across borders is lower than within a state. This suggests that the capacity to expand trade in areas where risk is an important factor will lag the expansion of the role of the market within borders. A corollary of this is that, while trade policy can legitimately be expected to open up markets where they exist, it probably should not be used to create markets where they do not exist, since this risks pushing societies faster and further than their internal frameworks for managing market-related issues can cope with.

Third, in areas where the idea of market-determined outcomes collides with deep ethical, social and political principles and values and where the pursuit of wealth must give way to other concerns – including health (physical life), culture (socio-cultural life) and environment (ecological life) – the interests of trade should by the same token defer to domestic preferences.

Fourth, reflecting the inevitability of eventually declining returns to more wealth, coupled with high positive income elasticities for "quality of life" factors such as health, richness of culture and a clean environment, the comparatively wealthy industrialized economies and comparatively income-poor developing economies will naturally have different preference structures. This suggests a multi-speed WTO for inclusion of trade-related "values" issues.

Fifth, social contracts are needed in any market-oriented society, even without trade, and the size of border effects gives scope to governments to maintain them in the presence of trade; accordingly, there is no barrier here to trade liberalization.

Sixth, WTO instruments should emphasize procedural rules and avoid building substantive rules into the body of hard-to-change WTO law.

Some Preliminary Considerations

A "first principles" perspective

Use of the market as the organizing principle for production at the national level permits, for well-known reasons, a much higher standard of living than does individual self-sufficiency. However, it raises several issues:

- It holds all individuals hostage to others carrying out their part in the division of labour, as well as making them dependent on the ability to participate in the division of labour.
- It opens the possibility of various types of "market failure" that would lead to inefficient outcomes.
- It overlays a powerful organizing framework based on individual choice on the underlying social, political and cultural systems and values of nation-states.

Nation-states have accordingly evolved social, political and economic regulatory frameworks that, respectively:

- control the risks to individuals implicit in the market-based organization of production and distribution (i.e. some form of "social contract");

- set out rules of the road (and establish institutions to enforce them) to promote efficiency in economic activity (i.e. economic and technical regulation); and
- contain the impact of the market on the social, political and cultural strata of the nation (what might be for convenience termed "social" regulation).

These frameworks are not static, as is shown by the recent history in the countries of the Organization for Economic Co-operation and Development of economic deregulation and privatization coupled with a parallel proliferation of social regulation concerning product standards, health and safety measures and environment. As Sylvia Ostry observes: "In the OECD countries social regulation started in the late 1960's and has been accelerating since then. The OECD has called the phenomenon 'regulatory inflation.' One could – with a bit of a stretch perhaps – say that the postwar economic regulatory state of the advanced countries is withering away, while the social regulatory state is alive, well, and growing: a curious mix of laissez-faire and laissez-regler."[1]

In retrospect, this is neither surprising nor paradoxical for two reasons.

First, the dismantling of economic regulation (which largely meant privatization and deregulation of the traditionally regulated sectors, namely telecommunications, transportation, finance and public utilities)[2] resulted in the externalization through social regulation of what had formerly been internal decision-rules, guidelines or simply tendencies engrained in the corporate culture of the state-controlled industries.

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[1] See S. Ostry, "WTO: Institutional Design for Better Governance," paper presented at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Center for Business and Government, Harvard University, June 1-2, 2000.

[2] This trend was the product of many factors. Some countries went this route out of conviction; some followed suit as a political economy consensus formed; some were pushed in that direction by competitive pressures and some by their financiers. An important underlying factor was the growth of the volume of information that had to be processed to manage systems of the size and complexity attained within industrialized economies at a time of rapid technological change. The volume of information simply swamped decision-making structures based on centralized command, control and co-ordination and led to the introduction of decentralized or, better,

Second, research and development was industrialized. This was embodied in newly minted armies of technological search engines (a.k.a. R&D personnel). This was facilitated by growth in the number of graduates of higher education, aided by the improvements in computer technology, motivated by the profit potential of new products and pushed by policy (e.g. "national innovation system" frameworks that encouraged universities and public research organizations to collaborate with industry). The result was an explosion of new products, each of which in some measure affected society, not only in a direct sense but also through possible interactions with other products. Each new product thus gave rise to a growing number of potential new regulations designed to control some aspect of its interaction with the social and economic system at large.[3]

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distributed decision making guided by general incentives and penalties (i.e. market-based systems).

[3] Whereas growth in the number of new products has been exponential in nature, potential interactions have grown at a combinatorial pace. Since combinatorial expansion dominates exponential growth the way that exponential growth dominates linear growth, the complexity of the economic system has soared. A good example is the history of interaction between the computer and the idea of a network. The idea of a computer network was first developed by the U.S. government to help government function in the aftermath of a nuclear war. Computer networks found their initial major application in supporting academic research collaboration, because it was universities that had mainframe computers. When the mainframe computer became ubiquitous within larger corporations, computer networks supported the fragmentation of production, which was manifest in the "outsourcing" wave of the 1980s. When the desktop computer, itself a spinoff from NASA's space program, became ubiquitous, the now well-established idea of a computer network gave rise to the World Wide Web. The modern Internet that emerged as a result interacts with virtually every aspect of society, creating almost boundless scope for potential new regulation. In different societies, the concerns will be different, as shown by the differences between, say, the United States and China in their responses to this phenomenon.

Given differences in resource endowments, stage of development, and historical influences on social, cultural and political structures, nation-states respond differently to technological and market developments. Accordingly, no two are identical in the specification of their economic regulatory frameworks, in the generosity of their social contracts, or in the breadth of scope given to the market. In short, each has a unique and continuously evolving policy "bundle."

Trade is nothing more than the extension of the market framework across national borders. This expands the potential gains from specialization and increased scale compared to what is attainable within individual states; at the same time, it also extends to the international dimension the issues raised by adoption of the market.

This has two basic implications. First, it brings the policy frameworks designed to deal with these issues at the national level into contact with one another. Second, it creates to some extent a need at the international level for policy and institutional frameworks analogous to those that exist at the national level.

While the set of international institutions to which this has given rise is extensive, it is nonetheless the case that domestic institutional and governance frameworks have been only partially and in many cases weakly replicated at the international level.[4] There is accordingly a very significant asymmetry in capacity to manage risk across borders as compared to within borders. This is undoubtedly one of the major reasons for the size of border effects and the extent of home bias in economic transactions that have been identified in the literature.[5] Moreover, it complicates matters considerably for a rules-based trade system since, while known risks might be dealt with in the context of trade negotiations as deliberate trade-offs in an exchange of benefits, it will be very difficult to get populations to accept new risks emanating from traded goods or services on the basis of past negotiations (which in effect would involve pre-commitments of unknown import). In other words, the acceptance of new products in trade will likely lag their acceptance at a national level, raising obvious difficulties for application of the precautionary principle.

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[4] In terms of macroeconomic issues, the International Monetary Fund (IMF) provides a lender of last resort to illiquid countries, the Paris and London Clubs provide an analogue of bankruptcy courts, and there have even been some efforts through the World Bank and the UN to replicate national fiscal mechanisms for cushioning regional terms of trade shocks. In terms of microeconomic issues, there are thousands of active committees under the International Organization for Standardization addressing technical matters. The United Nations Commission on International Trade Law (UNCITRAL) provides, through instruments such as the Convention on Contracts for the International Sale of Goods, the basis for settling contractual disputes between private parties. The Bank for International Settlements (BIS) and the International Organization of Securities Commissions (IOSC) provide a form of international financial supervision and regulation. UN-sponsored mechanisms have been formed to deal with

Given the uniqueness of the various national frameworks, they are generally not congruent to each other or to any international framework, other than minimalist frameworks based on the principle of the lowest common denominator. Any more ambitious framework, such as that developed for

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issues such as the impact of economic activity on climate change, status of women and indigenous peoples (impact of globalization on traditional life). And "economic" aspects of international crime such as drug trafficking and money laundering have also been dealt with one way or another internationally (including by the G-7/G-8). And the list goes on. The comparative weakness of international instruments is inevitable because the most powerful instruments available to deal with market issues, such as the power to tax (which is fundamental to addressing distributional issues) and legal enforcement and redress are prerogatives of the nation-state.

[5] The likelihood of a transaction taking place across borders is very small compared to a domestic transaction. See J.F. Helliwell, *Globalization: Myths, Fact and Consequences*, Benefactors Lecture, 2000, C.D. Howe Institute, October 2000. For a discussion of home bias and related empirical puzzles in international trade and investment, see M. Obstfeld and K. Rogoff, "The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?" *NBER Macroeconomics Annual 2000* (forthcoming).

international trade, thus inevitably gives rise to what Sylvia Ostry has labelled "system friction."[6]

Some of the relevant history

System friction was little in evidence in the early years of the General Agreement on Tariffs and Trade (GATT). Indeed, it has been argued that within the old GATT regime an implicit buffer had existed between international and domestic policy space. In this scheme, international rules restricted protectionist policies but did not dictate the content of domestic rules. This was not entirely true, but any exceptions (e.g. transparency requirements for publication and administration of trade regulations, a pre-WTO "exception to the paradigm of negative prescription") seem to prove the rule.[7]

The ambitious systemic reforms of the Tokyo Round clearly pushed the envelope in this regard. New instruments such as the Agreement on Technical Barriers to Trade (TBT) and the Agreement on Customs Valuation introduced requirements for positive regulation far more significant than transparency rules.[8]

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[6] See S. Ostry, "New Dimensions of Market Access: Challenges for the Trading System," in OECD, *New Dimensions of Market Access in a Globalising World Economy* (Paris: OECD, 1995); and *Governments and Corporations in a Shrinking World* (New York: Council on Foreign Relations, 1990).

[7] See W.A. Dymond and M.M. Hart, "Post-Modern Trade Policy: Reflections on the Challenges to Multilateral Trade Negotiations after Seattle," *Journal of World Trade* 34(3), 2000, p. 23, especially footnote 2.

[8] Dymond and Hart downplay the significance of these measures in comparison to later Uruguay Round developments, arguing that the GATT did not require any country to have a tariff regime (which would trigger the customs valuation requirements) or to have product standards (which would trigger the TBT provisions). Ibid., p. 24. Since most countries have tariffs and product standards, this argument is largely moot. These agreements did require domestic regulation in a de facto, if not a de jure, sense. Moreover, while the positive regulation introduced in the Tokyo Round was mostly procedural rather than substantive, even procedural regulation can have significant implications in terms of infrastructure requirements

Notably, both of these particular agreements also contained preambular statements of intent to achieve harmonization of standards. Moreover, other new instruments on subsidies and government procurement gave the GATT's national treatment provision newly found leverage inside national borders.

And system friction started to be seen: one example was the 1982 ruling by a GATT panel that a number of instruments used by Canada to exact performance requirements from foreign investors violated Canada's national treatment obligations; another was the European Community complaints at the GATT in the 1980s about Japan's close government-business relationship, perhaps the quintessential example of system friction.[9]

The Uruguay Round pushed the envelope still further: important innovations included: (a) the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), which requires WTO members to comply with, *inter alia*, the Berne Convention; (b) the General Agreement on Trade in Services (GATS), which *inter alia* requires members to establish mechanisms to review administrative decisions affecting service providers; (c) the Agreement on Sanitary and Phytosanitary Measures (SPS), which requires demonstrable scientific support for measures; and (d) the Agreement on Agriculture, which elaborates rules on domestic support for producers. As Dymond and Hart argue, "Taken together these agreements, combined with the positive obligation to ensure conformity with WTO rules, the new powerful dispute settlement system, and the trade policy review mechanism, institutionalize a degree and intensity

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(e.g. administrative procedures law as well as highly trained physical and social scientists); as Sylvia Ostry has pointed out, these were particularly burdensome for developing countries. See S. Ostry, "WTO: Institutional Design for Better Governance," op. cit.

[9] See W.A. Dymond and M.M. Hart, "Post-Modern Trade Policy," op. cit., pp. 23-24 and pp. 28-29.

of intervention into domestic governance which exceeds anything possible or contemplated under the GATT."[10]

There was still a further departure taken in the Uruguay Round from the traditional GATT approach to liberalization. The basic approach of the GATT was *symmetrical lowering* of trade barriers to *asymmetrical levels* (an approach that respected differences in initial conditions in the various GATT members). The TRIPS agreement involved *asymmetrical lowering* of barriers (or reform of rules, as was the case in TRIPS) to *symmetrical levels* or uniform provisions. The latter approach does not respect differences in domestic conditions in member countries and finds no support in economic theory or empirical research.[11]

And last but not least, the creation of an independent Appellate Body elevated the dispute settlement mechanism (at least in the view of some) to a form of international constitutional law. For example, Robert Howse and Kalypso Nicolaidis observe that the WTO "is often claimed to be performing constitutional functions, or to be an incipient global economic constitution." They add: "The proponents of a constitutional understanding of the WTO point to the new binding, juridically rigorous dispute settlement mechanism… [and] the explicit role such tribunals play in balancing competing public values, economic efficiency vs. health and safety goals for instance, in the scrutiny of domestic regulation."[12] In a similar vein, Sylvia Ostry writes: "Inevitably the dispute panels and especially the Appellate Body have been forced to interpret the relevant WTO rules. And inevitably, as is the case with all courts and all legal rules, but even more so because some WTO rules are deliberately imprecise or 'creatively ambiguous', the interpretation has essentially involved these internationally appointed judges making law, i.e. defining the boundary for domestic policy space and reinforcing the perception – and reality – of the intrusive nature of the new system."[13]

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[10] Ibid., p. 26. It should be noted that there are examples of far more onerous intrusion into domestic policy space outside the world of trade – for example, conditionality applied by the IMF and World Bank (whereby positive regulatory reforms are required to qualify for loans). Unlike the intrusions of trade rules, conditionality is discretionary and has far greater scope for diminution of national sovereignty.

[11] See J.D. Gaisford and R.S. Richardson, "The TRIPS Disagreement: Should GATT Traditions Have Been Abandoned?" in *The Estey Centre Journal of International Law and Trade Policy*, Vol. 1, No. 2, 2000.

[12] For a discussion and sources, see R. Howse and K. Nicolaidis, "Legitimacy and Global Governance: Why Constitutionalizing the WTO Is a Step Too Far," paper presented at the conference *Efficiency, Equity and*

But this understanding of the significance of the Uruguay Round innovations in the area of dispute settlement must be tempered by consideration of the comparative effectiveness of the old GATT mechanism, which (as has been observed by a number of commentators) is somewhat of a mystery. On the face of it, the GATT process was entirely toothless since the positive consent of the disputing parties was required both to begin the process and to accept its results. Yet it resulted in many panel decisions, most of which were adopted and, despite the absence of an orderly regime of sanctions, generally complied with. Moreover, it was not necessarily less used than the new dispute settlement under the WTO: while the number of cases has risen since GATT days, so has the number of member states and the volume of trade. Taking these latter scaling factors into account, the WTO mechanism has arguably been no busier than its GATT predecessor. The success of GATT

Legitimacy: The Multilateral Trading System at the Millennium, Center for Business and Government, Harvard University, June 1-2, 2000. Insofar as the WTO has actually assumed such a role, this is an unintentional outcome. As Debra Steger writes, "Uruguay Round negotiators did not intend to create a strong, new international court responsible for resolving trade disputes. Rather, their objective was to provide a security blanket or a 'safety valve'...to ensure against bad decisions of panels, as part of the *quid pro quo* for automatic adoption of panel reports by the DSB." See D. Steger, "The Appellate Body and Its Contribution to WTO Dispute Settlement," paper presented at the conference *The Political Economy of International Trade Law*, University of Minnesota, September 15-16, 2000.

[13] See S. Ostry, "WTO: Institutional Design for Better Governance," op. cit.

dispute resolution is often attributed more to GATT culture than to the design of the process or the leverage of trade. This suggests, at a minimum, that the comparative success of the GATT/WTO dispute settlement system does not rely entirely on the coercion implicit in suspension of trade benefits.

To summarize the discussion of the evolution of trade rules:

- The early GATT did not intrude much into domestic policy, although neither was it pure in this regard; moreover, it already contained significant potential for intrusiveness through the national treatment provision.
- Tokyo Round measures introduced positive regulatory requirements and gave new-found leverage to the national treatment provision. While mainly procedural in content, the new measures signalled in their preambular statements the objective of harmonization of rules.
- The Uruguay Round multiplied the number of agreements with positive regulatory requirements, introduced substantive regulation in addition to procedural regulation, made in one case the further leap to symmetrical final levels (i.e. harmonization) and introduced constitutional overtones into the rules-based multilateral system.

Seen in this light, the Uruguay Round was not quite as radical a departure as is often suggested; rather it appears to be an expansion of, and follow-through on, the breakthroughs achieved in the Tokyo Round, and in some sense the unfolding of a potential nested in the original GATT.

Thus, where "first principles" considerations lead to the conclusion that system friction is inevitable and that some accommodation of national rules to international standards is unavoidable if the full potential of trade to expand welfare is to be tapped, the history of the GATT suggests that this has always been implicit in the framework of multilateral rules and, moreover, has been "in the works" for several decades, going back at least as far as the Tokyo Round in the 1970s.

If system friction is indeed an inevitable consequence of the maturation of an international economic system, the questions then become: which rules to harmonize, to what extent, and with what implications for compromise of national objectives?

There are several pertinent observations here.

First, there is the empirical fact that "borders matter." Moreover, borders matter much more for services trade than for goods trade.[14] This may reflect the fact that services trade liberalization has lagged goods trade liberalization or the possibility that the importance of "localness" is far more important for services transactions, which is where the concerns about compromise are concentrated, than for goods purchases. One way or the other, the impact of trade on regulatory choices domestically (out of concern for possible competitive impacts on domestic industry), even in the context of highly integrated pair countries such as Canada and the United States, is as yet comparatively small.

Second, while trade negotiations and trade disputes by design constrain regulatory choices in terms of *how* to achieve given domestic policy objectives, whether or not they compromise the actual attainment of basic policy goals (e.g. either by ruling out the only technically feasible means or by ruling out the only financially feasible means) needs to be empirically demonstrated. These issues are addressed below.

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[14] In a Canada-U.S. context, the likelihood of a cross-border intercity transaction involving goods has fallen from being some 20 times smaller pre-FTA than a similar transaction on one side of a national border to about 12 times smaller since the FTA. For services transactions, the likelihood was not much changed by the FTA and remains at over 30 times smaller than for an intranational transaction.

The Interface with Norms and Values

The areas where it is usually held that social norms and values are under pressure because of trade are the "usual suspects" of health, culture, the environment and labour standards. Each of these is a general rubric that subsumes a number of major and minor issues. A full discussion of each would be beyond the scope of this note; the discussion below seeks only to identify a few commonalities that might be the basis for useful principles in dealing with the various issues.

Trade and health

Trade and health has at least two major groups of issues that warrant comment in the present context: product safety issues, which are handled under the SPS Agreement and which currently feature in the debate over the precautionary principle; and trade in health services under the GATS, where controversies relate to the possible impacts that trade could have on national health services systems.

On the product safety issues, the key point raised in the preceding discussion is the asymmetry of the scope for risk management across borders compared to within a nation-state. Absent this asymmetry, and using domestic thresholds for acceptability of risks in a trade context seems eminently reasonable and makes resistance to accept these risks in a trade context seem protectionist. However, given the asymmetry, maintaining a higher threshold of acceptability of risk in trade than domestically seems less unreasonable.

Turning to the health services industry issue, this sector has enormous economic potential and therefore trade potential; yet trade volumes are relatively low, liberalization is little in evidence and governments are dominant in the sector.[15] The reasons are well known:

- From a society's perspective, health has public good characteristics (with large positive externalities from good health and even larger negative externalities from disease, especially contagious disease).
- From the individual's perspective, health care is a basic necessity, a need not a want. Accordingly, ensuring adequate health care is an explicit, high-priority policy objective of most governments, quite independent of economic circumstances and goals.
- Moreover, there is an asymmetry of information between patients and health care providers, a circumstance that typically triggers regulation and supervision and constrains the role of the market.[16]
- More deeply, health is an area where notions of fairness and equality come into play strongly, indeed with overriding force (i.e. access to health care should not be based on ability to pay). As Gary Hufbauer has observed, societies may have largely reconciled themselves to great disparities in income, as the price to pay for having a wealthy society; however, societies may not be ready to accept similar large disparities in health outcomes.[17]

This does not preclude a role for markets either in developing health care as an industry (including explicitly for trade purposes by putting to good use excess supply where it exists for reciprocal provision of health care to non-residents) or in managing access through private sector insurance plans. Nor does it necessarily preclude for-profit competition by foreign services suppliers through the various GATS modes: providing hospital/medical services a commercial presence in domestic communities, through movement of natural persons, or on a cross-border basis through "telehealth" service delivery.

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[15] See J. Vellinga, "International Trade, Health Systems and Services: A Health Policy Perspective," in J.M. Curtis (ed.), *Trade Policy Research 2001*, Department of Foreign Affairs and International Trade, Ottawa, December 2001.

[16] Ibid.

[17] See G. Hufbauer, "Trade and Coherence: Where the Major Gains Lie," in *Trade Policy Research 2001*, op. cit.

However, there are many issues to be resolved before there would be comfort in many developed societies with a significant role for the private sector (and by extension for trade). These include:

- dealing with the moral hazard and adverse selection issues implicit in insurance systems, without at the same time undermining the objective of universal access;
- providing assurance of supply and of standards, which can be compromised in an industrial model when profits are squeezed and the industry faces market consolidation and cost containment pressures;[18]
- dealing with cross-border risk management issues, which include, *inter alia,* coverage of doctors against malpractice suits mounted in courts abroad; recognition of credentials earned abroad; and the risk of gaps in supply created by withdrawal of foreign providers (which would appear to be greater than the risk of domestic health care personnel moving abroad, yet another complicating asymmetry).

These are not problems of principle but of practicality. Nonetheless, the practicalities are sufficiently problematic that most industrialized countries maintain regulated systems for principal health services that feature more or less universal insured coverage, comprehensive coverage of benefits, income-based contributions, and administrative mechanisms to control costs; and few WTO members have made liberalization commitments under the GATS (Canada made none).

While the expansion of international trade in health services may be inevitable, as Vellinga concludes, the record to date within the OECD is that government involvement in the health sector increases as national per capita incomes rise.

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[18] Evidence of this has been found in the U.S. managed health care system: "Pressure to protect profit margins has led to such dubious business strategies as the avoidance of sick patients, the excessive micromanagement of physicians, the worsening of staff-to-patient ratios, and the outright denial of care." See Vellinga, op. cit., p. 171.

The bottom line here appears to be that the benefits delivered by the market system in terms of efficiency tend to be secondary to more basic health policy objectives of preserving life and health; accordingly, the role of the market (and therefore of trade) is likely to remain circumscribed. Moreover, given the asymmetry in cross-border versus domestic management of risks, this is an area where the expansion of trade is likely to lag any expansion of the market in a domestic context, and the interests of trade will likely have to defer to domestic concerns.

Trade and culture

In his review of the recent literature on trade and culture, Bruce Jamieson considers how trade liberalization affects cultural industries, how it impacts on the legitimacy of the nation-state as a repository of distinctive, common cultural values, how it impacts on national identities, and what might be its longer-term impact on social cohesion.[19] Jamieson concludes that cultural goods and services are not like other goods and services and that cultural diversity is preferable to homogeneity. This lays the basis for a role for governments to play in promoting and preserving cultural diversity and specifically at ensuring space for "Canadian voices telling Canadian stories."

This general notion is put into a framework that is tractable from the perspective of trade and economic policy through the observation that "the instruments of communication of this culture [are] the cultural industries."[20] These include, variously,

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[19] See B. Jamieson, "Trade Liberalization: Culture, Identity and Social Cohesion," in *Trade Policy Research 2001*, op. cit.

[20] Department of Communications, *Vital Links: Canadian Cultural Industries* (1987). This notion is consistent with the community development/animation model of cultural policy that emphasizes the value of community self-knowledge and thus centres on the media that reflect the

"high culture" (opera, ballet and the fine arts); "ethnic culture" (folklore, traditional arts and architecture); and "popular culture" (film, theatre, television, music, mass-market books and mass-market periodicals). These industries serve a dual function: to individuals they provide information, entertainment, intellectual stimulation and so forth; for society they create shared ideas, condition shared attitudes, foster shared habits and shape shared opinions, all of which are important in one way or another to cultural identity and thus, by this theory, to social cohesion.[21] This dual function appears to be at the root of the notion that cultural goods and services are "different" from other goods and services.

In an industrial setting, cultural policy is delivered through industrial policy, cultural objectives become synonymous with domestic market output, and trade in cultural products becomes

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community's image back to its constituents. There are alternative policy models, including promoting creation of, and access to, works of "high" culture (both national and international), preserving national heritage (including both artifacts and values) through publicly funded institutions, and promoting development of merit goods by popular culture industries. These are reviewed in B. Jamieson, op. cit.

[21] Insofar as there is any valid connection between media feedback of a given culture to its host society and social cohesion, this would be a powerful argument in support of a cultural policy delivered through the mass media, since social cohesion has been persuasively argued to have positive effects on the efficiency of economies, quite apart from the purely social benefits. However, the most widely cited economic theory of the link between social cohesion and economic performance, namely from Robert Putnam, bases this linkage on informal, purely local social interaction stimulated by membership in choral societies, bowling leagues, etc. This has little to do with "audiences" or the mass media (and arguably mass media are inimical to this concept of social cohesion, since they tend to displace active social participation with passive "audience" behaviour). It can further be observed that any self-referential feedback changes and distorts a system in unpredictable ways. Accordingly, while it is certain that Canadian cultural feedback will produce a different result than broadcast American influences, what that result might be is neither predictable nor controllable, simply different (e.g. it is not unreasonable to presume that the popularity of the rather belligerent "Joe Canadian" ads is in part a response to the "boy scout" images of Canadians that had dominated Canadian cultural feedback).

a source of trade-offs: opening up provides individuals the benefit of expanded choice and cultural producers with expanded markets; but the ensuing cultural spillovers associated with imports must then, by this theory, be taken to diminish cultural distinctiveness (and, by implication, social cohesion, if one accepts this part of the thesis).

The outline of the trade and culture issue sketched above is only part of the story. An important overlay is the perceived threat to local distinctions posed by globalization, of which trade is of course but one agent. By allegedly eradicating the distinctions that make us "us," globalization is equated with homogenization, which in turn means cultural destruction.[22] This sense of threat to local distinctions generates negative reactions that reverberate through the trade system and specifically against globalization's corporate iconography.

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[22] As Salman Rushdie has famously put it, globalization is an attack on "the world's precious localness: the Indianness of India, the Frenchness of France." The threat of homogenization, and associated calls for preservation of cultural diversity, is a recurring theme in the literature reviewed by Bruce Jamieson. See B. Jamieson, op. cit. Concern over homogenization is actually pure hyperbole. The concept has no practical meaning within national borders, and the extent of border effects discussed earlier is a guarantee of the persistence of distinctive traits from nation to nation. The sense of cultural diversity under threat is also hard to square with the historical evidence of the survival of distinct cultures under far more adverse circumstances than those posed by mere trade in goods and services. The world has seen survival of suppressed cultures (e.g. Greek culture under centuries of Ottoman rule), of stateless cultures (Basque culture and language), of purely local cultures (ranging from the persistence of features of cities such as the distinctively different *arrondissements* of Paris to regional dialects and accents), and of specific elements of particular cultures under different influences (Chinese *guanxi* has survived the Cultural Revolution on the mainland, British rule in Hong Kong, Portuguese rule in Macau and American influence in Taiwan). The idea of homogenization through the media is equally hard to square with the flourishing of wildly different subcultures within the most media-saturated corner of the world, the United States itself.

However, cultural convergence is a very real feature of globalization, as evidenced by the proliferation of common elements even within very distinct societies. Equally real is the acceleration of cultural evolution due to the combination of globalization and intense feedback from mass media. Both convergence and accelerated evolution are destructive of traditional cultures, which is very likely the root of the concern voiced over "homogenization."

Recognizing the sense of threat abroad, Jeffrey Garten, currently Dean of the Yale School of Management and a former undersecretary of commerce for international trade, has written, "The U.S. should do more than heed these warnings [of the impact of globalization on local cultures]; it should recognize that strong cultures are in America's self interest. If societies feel under assault, insecurities will be magnified, leading to policy paralysis, strident nationalism and anti-Americanism."[23]

One approach that has been promoted to deal with the *sui generis* problems associated with trade and culture is a new international instrument on cultural diversity. To be useful in a trade context, such an instrument would have to provide a basis for sorting out what cultural policies were to be safeguarded from trade disciplines (or alternatively, in what contexts cultural policies would be deferred to in trade rules). This would seem to require more than a minimalist affirmation of the value of cultural diversity. Yet given the fact that the world *is* culturally diverse, achieving a common vision on such a fine delineation of the scope of international trade rules seems too much to realistically hope for.

An alternative approach would be a sectoral agreement that would include cultural and entertainment goods and services within the framework of the WTO with special provisions for particular circumstances – similar to the approach taken for telecommunication services, where a reference paper set out the definitions and principles for the sector's peculiarities.[24] While the development of such an agreement would be complex and difficult, it would have the advantage of necessarily spelling out the management of specific practical issues, which a more general instrument on cultural diversity outside the WTO would not provide. Such an instrument would likely be possible to negotiate only in the context of a round, unless the "critical mass" approach taken with the telecommunications agreement were adopted (an approach that might not be viable in this instance, given that the country that would stand to face the most constraints, the United States, would not likely come on board except on the basis of important offsetting benefits elsewhere, if ever).

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[23] Cited by Hilary Mackenzie, "Commodity vs. Culture: Battle Lines Are Drawn: It's a Challenge to Keep a Separate Canadian Identity in the Era of Global U.S. Pop Culture," *Ottawa Citizen,* March 16, 1999.

[24] Such an approach has been advanced by Keith Acheson and Christopher Maule. For a discussion and sources, see B. Jamieson, op. cit.

Given the hurdles that either of the above approaches faces, there is a distinct possibility that, for the foreseeable future, cultural policies will have to fend for themselves within the current international trade law setting. On the face of it, this would leave cultural policies at some risk (especially insofar as they are identified with domestic industry interests, as they are in Canada). This reflects the fact that there is only one explicit safeguard for cultural policies in the GATT (a provision in respect of cinematographic films) plus the general exceptions provided for under Article XX, which might be hard to apply:

- For example, any trade dispute is likely to be in connection with the mass popular media, which are both the prime source of reinforcement of cultural identity according to the cultural transmission theory and the area where commercial interest, including trade interest, is highest.
- Second, there is no evidence that *any* nation is prepared to restrict the export of its own culture in order to allow other nations to preserve their own; quite the reverse – nations take great pride in their artists and cultural industries and actively promote their works abroad. In this context, protestations that restrictions on imports of cultural products are required for higher social goals are bound to sound hypocritical.
- Third, the standard economic concepts that underpin trade (comparative advantage across geographic areas, specialization and division of labour between countries, etc.), as well as the basic principles of trade policy (such as national treatment), are of little help in arriving at broadly acceptable solutions that balance import and export interests because they simply make no sense when applied to

"cultural" goods and services, the basic distinguishing characteristic of which is precisely where or by whom they are produced.

- Further, distinctions between cultural products based on nationality will often strain credulity because anything that might be identified as a cultural good or service is more likely to be associated in a geographical sense with what might be termed a "civilization" than with a national "culture."[25] This is particularly the case with any cultural product aimed at the global market.
- In a similar vein, the virtual impossibility of establishing in objective terms the point at which cultural imports start to erode cultural identity or impair social cohesion makes it difficult to disprove protectionist intent in a trade dispute context.

Indeed, in the only instance in which a cultural policy was challenged (Canada's split-run magazine policy), the policy was ruled WTO-inconsistent, despite the comparatively small share of the Canadian magazine market controlled by Canadian product. Among the important factors that contributed to this result were:

- numerous statements by Canadian policy makers affirming the protectionist intent of the policy (a direct result of the identification of the cultural policy with industry interests);[26]
- the difficulty of clearly showing a distinction between "Canadian" content and foreign content;[27] and

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[25] For example, there is nothing distinctively "Canadian" about Glenn Gould's very distinctive rendition of the *Goldberg Variations*, although the recording is a product of the Canadian cultural industry, being recorded by a Canadian in a Canadian recording studio. Few would disagree, however, with this work being labelled a product of "Western civilization."

[26] For example, see the Appellate Body's discussion of this issue in *Canada – Certain Measures Concerning Periodicals: Report of the Appellate Body*, WT/DS31/AB/R, June 30, 1997, at p. 33. Here the Appellate Body cited various official Canadian statements that affirmed the intent to protect.

[27] Here the argument turned on the question of whether the products were "like," which in turn depended on whether they were "competitive."

- the stringency of the criteria for applicability of the Article XX exceptions, which require in particular that the exception be necessary to comply with another WTO-consistent law, which would be typically the case in an environmental law context but would not make much sense in a cultural policy context.[28]

At the same time, it needs to be borne in mind that this was the *only* such case in WTO history, despite the wide range of products that might be considered as "cultural" that are actively traded. Moreover, the ruling went only to the means and not to the cultural objective; in fact the panel went to some pains to emphasize that the objective of the cultural policy was not at issue, only the WTO-consistency of the mechanisms devised to achieve it.[29] This would be a very narrow base indeed from which to argue that cultural policies are being threatened by trade rules, despite the absence in the trade rules of provisions on which deference to cultural policies could readily be based.

Trade and the environment

The trade and environment debate represents well-trodden turf. As Steve Charnovitz has pointed out, this issue goes back at least to 1925 when William Smith Culbertson, one of the architects of America's trade reciprocity policy, suggested that "Following, or perhaps as part of, a conference on commercial policy [i.e. most favoured nation rules, unfair competition, market access, investment, etc.], there should be held a world

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The Appellate Body cited various official Canadian statements that emphasized the competition between Canadian and U.S. magazines. Ibid., pp. 29-30.

[28] See the argument of the Panel on this issue at paragraphs 5.7 to 5.9 in *Canada – Certain Measures Concerning Periodicals: Report of the Panel*, WT/DS31/R, March 14, 1997, pp. 75-76.

[29] Ibid., at paragraph 5.9, p. 76.

conference on the conservation of natural resources."[30] Moreover, there has been considerable initiative in this field with 20 multilateral environmental agreements (MEAs) currently in force that include trade-related measures.[31]

Nonetheless, there is no evident consensus regarding the functional links between the two issue areas, let alone consensus on the broader normative aspects.[32]

The fact that this issue area remains so active despite its long history and the prolific analytical literature that it has stimulated reflects in large part the fact that it is very complicated and there are many strands to the discussion. For example, trade has been linked in one way or another to a wide range of environmental problems: pollution, resource depletion, global commons issues, endangered species, solid and hazardous wastes, and reduction of biodiversity. Moreover, the underlying analytical issues vary across the issue areas; they include spillovers/externalities of various types, problems of the commons, intertemporal problems, uncertainty and information deficiencies, and reversibility/irreversibility of consequences. Further, the role of contributing and contextual factors varies from issue to issue as well; these include the quality of definition and enforcement of property rights, the adequacy of regulatory capacity, poverty and stage of development, and governance issues of various types (including the possibility of misguided policy due to factors such as interest group pressures,

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[30] See S. Charnovitz, "Living in an Ecolonomy: Environmental Cooperation and the GATT," paper prepared for the *Conference on Trade and the Environment*, Pacific Basin Research Center, John F. Kennedy School of Government, Harvard University, April 29-30, 1994.

[31] These 20 are a small subset of the overall set of 200 MEAs; the fact that the vast majority of MEAs do not contain trade provisions should not go without notice.

[32] More than one commentator has called the trade and environment debate a "dialogue of the deaf," and few see much progress in the WTO's Committee on Trade and the Environment (CTE). See, for example, W.A. Dymond, "Environment and Trade: Lessons of the MAI," Department of Foreign Affairs and International Trade (mimeo).

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short-run focus, poor analysis, etc.). As well, the level at which the various issues are tractable varies from subnational governments to national governments to regional groups and multilateral organizations. Finally, the linkage between trade and the environment is also "complex" in the sense of there being important interactions across issue areas (e.g. the well-known interplay between deforestation, reduction in biodiversity, poverty and property rights).

For the purposes here, it is useful to start by examining the cases where trade *rules* and environment have actually come into conflict. In point of fact, the number of GATT/WTO cases in which environmental measures have been challenged is not very large at all. The WTO lists altogether eight disputes over environmental measures during the history of the GATT/WTO:[33]

- *United States – Prohibition of Imports of Tuna and Tuna Products from Canada.* In this 1982 case, Canada successfully challenged a U.S. restriction on imports of tuna from Canada that had been imposed as retaliation for Canadian authorities arresting U.S. fishing boats trawling illegally in Canadian waters.
- *Canada – Measures Affecting Exports of Unprocessed Herring and Salmon.* In this 1988 case, the United States successfully challenged Canadian export restrictions of unprocessed herring and salmon that Canada claimed were part of a system of fishery resource management aimed at preserving fish stocks.
- *Thailand – Restrictions on the Importation of and Internal Taxes on Cigarettes.* In this 1990 case, the United States

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[33] Source: WTO website, Environment Disputes. A broader interpretation of what constitutes an environmental case would expand this list somewhat. For example, the recent dispute between Canada and Australia over the latter's ban on salmon imports had an environmental element insofar as the Australian measures were ostensibly for quarantine reasons to prevent the introduction of certain salmonid diseases into local fisheries.

successfully challenged a Thai import restriction on cigarettes based on a claim that chemicals and other additives contained in U.S. cigarettes might make them more harmful than those in Thai cigarettes.

- *United States – Restrictions on Imports of Tuna (Tuna-Dolphin).* In this 1991 case, Mexico and others challenged U.S. restrictions on imports of tuna from countries that did not meet U.S. environmental regulations designed to safeguard dolphins from tuna nets. The panel found against the U.S. ban on grounds of extraterritorial application of domestic laws but upheld as GATT-consistent the U.S. policy of requiring tuna products to be labelled "dolphin-safe" (leaving to consumers the choice of whether to buy the product). As it turned out, the report was not adopted (and so is not part of GATT/WTO law); Mexico and the United States negotiated a bilateral settlement.
- *United States – Restrictions on Imports of Tuna (Tuna-Dolphin II).* In this 1994 case, the European Union brought a similar challenge, again without resolution. Although the panel again found against the United States, the dispute lapsed with the transition from the GATT to the WTO.
- *United States – Taxes on Automobiles.* In this 1994 case, the EU challenged three U.S. tax measures: luxury and "gas guzzler" taxes on automobiles (which applied respectively to cars sold for over $30,000 and those attaining less than 22.5 miles per gallon) and the so-called Corporate Average Fuel Economy (CAFE) regulation, which required the average fuel economy for passenger cars manufactured in the United States or sold by any importer not to fall below 27.5 miles per gallon. Companies that were both importers and domestic manufacturers had to calculate average fuel economy separately for imported passenger automobiles and for those manufactured domestically. While the panel found the first two measures GATT-consistent, it found the separate accounting requirement for imported cars under the

CAFE regulation to be discriminatory. In any event, the panel report was never adopted.

- *United States – Standards for Reformulated and Conventional Gasoline.* In this 1995-1996 case, Venezuela and Brazil successfully challenged U.S. rules on the chemical characteristics of imported gasoline on grounds that these were stricter than the rules for domestically refined gasoline.
- *United States – Import Prohibition of Certain Shrimp and Shrimp Products (Shrimp-Turtle).* In this 1997-1998 case, India, Malaysia, Pakistan and Thailand successfully brought a joint complaint against a U.S. ban on imports of shrimp caught without U.S.-specified safeguards for endangered sea turtles. While the WTO ruled that measures to protect sea turtles would be legitimate under GATT Article XX, it ruled against the United States because the measures in question discriminated between WTO members, providing countries in the western hemisphere – mainly in the Caribbean – technical and financial assistance and longer transition periods for their fishermen to start using turtle-excluder devices than it did to the complainants.

Several observations are warranted. *First,* quite remarkably, the United States has been involved in each and every case, in all but two as the party being taken to the WTO, a fact that may explain the relatively high profile of this issue. *Second,* while the party defending the environmental measure consistently lost, the grounds were, variously: (a) extraterritorial application of its own laws (*Tuna-Dolphin*); (b) discriminatory application of environmental measures that were otherwise upheld as valid (*Shrimp-Turtle*, *Reformulated Gas*, *CAFE*); or (c) unauthorized retaliation (*United States-Tuna*). None of the cases spoke to the merits of the environmental objectives of the disputed measures. *Third,* no measure implemented pursuant to any of the multilateral environmental agreements that contain trade-related provisions has been the subject of a trade challenge under the GATT/WTO. *Fourth,* most of the cases are recent; in fact, all but two were brought in the 1990s toward the end of a period of significant expansion of environmental and other regulation in the OECD countries. *Fifth,* and further to the preceding point, the number of environmental cases brought forward as a fraction of the number of environmental regulations that have been instituted globally is vanishingly small; bearing in mind the frequent presence of scope, and the not inconsiderable temptation, to use environmental regulations for covert protectionism, not to mention the ever-present scope for plain vanilla poor regulatory design, this is mildly astonishing.

Taking the various points together, there simply is no "smoking gun" here of trade rules undermining environmental regulation in the developed countries or of developed-country environmental regulations being successfully used for covert "green protectionism." Clearly, trade rules constrain the choice of regulatory design and therefore challenge to some extent the cleverness of regulatory authorities; however, the real challenge to cleverness in designing regulations would seem to be not in crafting environmental rules that are not discriminatory in a trade sense but rather in devising rules that are both environmental *and* effectively trade-protectionist.

Turning from the impact of trade rules to the impact of trade itself, it has been argued that trade impacts on environment through "regulatory chill" (environmental regulations not enacted because of competitiveness pressures stemming from trade); and by prompting a "race to the bottom" (the gutting of once-stringent regulations to compete with jurisdictions with weaker regulations). Both arguments depend on there being a powerful harmonizing influence on domestic regulation from trade or the potential of trade (or alternatively the movement of production to the territory of environmentally lax regimes). However, the message of the evidence that "borders matter" is that there is no such powerful harmonizing influence and that states have considerable leeway to enact social regulation of their choice. This alone leads to the expectation that empirical evidence would be lacking for either hypothesis. In point of fact, while the "regulatory chill" argument, being a statement concerning a counterfactual circumstance (what would have prevailed absent trade), is neither provable nor disprovable, the "race to the bottom" argument appears to be flatly at odds with the proliferation of environmental regulation in OECD countries. In his survey of the literature on trade and environment issues, Rob Stranks concludes that neither contention has been supported by the evidence.[34]

Where then is the source of the heat in this debate? Controversy usually follows hot on the heels of failure. For the most part, the problem here appears to be not what was done but what was *not* done – in particular to prevent damage to the global commons. There is little disagreement with the contention that the "global commons" have not been well protected or managed: examples often cited include the depletion of the ozone layer, climate change, the extinction of species, pollution of the most remote ecosystems, and the collapse of major fisheries based on migratory fish stocks.[35]

While the operation of trade rules is not implicated in this failure (global commons are the subjects of MEAs and, as noted earlier, no action taken pursuant to any MEA has ever been challenged in the WTO), the role of trade has been so implicated through the "ecological footprint" argument.[36] This thesis applies the same logic as underpins the tradable permits approach to meeting global emissions reduction targets, namely that ecological deficits in some countries (e.g. emission of more carbon dioxide than the national carbon sinks can absorb) can be balanced by ecological surpluses in others.

To many, this is a question of good governance; and indeed, insofar as environmental issues involve quantifiable externalities, they should indeed be tractable through good governance.[37] However, in a context where exhaustible resources are not priced appropriately by market economies,[38] where not all nations have adequate environmental regulations,[39] and where inadequate measurement and partial accounting frameworks leave public sector managers in effect "flying blind" as to actual levels of ecological stress,[40] trade may allow – and indeed encourage – unsustainable growth.

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[34] See R. Stranks, "Trade and Environment: Post-Seattle Looking Forward," in *Trade Policy Research 2001,* op. cit.

[35] For a discussion of the role that this plays in the issue of civil society participation in the WTO, see J.M. Curtis, "Trade and Civil Society: Toward Greater Transparency in the Multilateral Trade Process," in *Trade Policy Research 2001*, op. cit.

[36] See, for example, Mathis Wackernagel et al., *Ecological Footprints of Nations: How Much Nature Do They Use? – How Much Nature Do They Have?* (http://www.ecouncil.ac.cr/rio/focus/report/english/footprint).

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[37] Bagwell and Staiger argue that the WTO may be well suited in its current form to help manage the pecuniary externalities associated with choices over environmental standards. Insofar as the problem is an incentive to shift protectionist pressures from tariffs, which are subject to disciplines, to labour and environmental standards, which are not, they argue that, "governments can maintain the right to unilaterally determine their own domestic standards without sacrificing global efficiency *provided that they face appropriate restrictions on their choices which offset this incentive"* (emphasis added). See K. Bagwell and R.W. Staiger, "Domestic Policies, National Sovereignty and International Economic Institutions," *Working Paper 7293*, NBER; available online at http://www.nber.org/papers/w7293

The application of this approach depends to some extent, however, on the market concepts of tastes and preferences in respect of risk-return. For example, if one can frame the issue of, say, environmental protection in terms of tastes or preferences, then the application of the general body of social choice literature leads to the legitimacy of choices that result in some measure of environmental damage. Different populations will have a different intensity of preference or "taste" for clean air or clean water; in such instances, market instruments (e.g. application of the polluter pays principle) are suggested to deal with the externalities flexibly so as to maximize welfare. However, it is hard to think of a "taste" for more or less species extinction; accordingly, there are limits to how far this notion of good governance can be pushed.

[38] This is a generally unassailable proposition since market pricing reflects the time preferences of individuals of the current generation and thus favours more short-term consumption than would be the case if the time preferences of societies, which being of indefinite longevity would discount future consumption much less than do individuals, dictated consumption choices.

[39] For example, taking the case of rain forest habitats of orangutans and the international plywood market, an unmistakable global choice is being made at the present time in favour of cheaper plywood at the expense of orangutans, in some measure due to inadequate regulation in countries that harbour orangutans. From the orangutans' point of view – as well as from the perspective of those who form a political constituency on their behalf – trade is therefore very much a part of the problem – even if, as in pretty much all such cases, trade is but one factor among many (e.g. in this case, *lebensraum* population pressures are also a major factor).

The theoretical link posited by the ecological footprint argument is therefore cogently framed; the policy implications then turn on the question of where the planet is vis-à-vis its "carrying capacity," an issue well beyond the scope of the present paper. The extent to which trade policy can be a useful tool to address issues of this type, however, does need to be addressed and will be dealt with later in this paper.

Trade and labour standards

The issue of trade and core labour standards also has several characteristics that are pertinent here. Core labour standards can embrace various wage and workplace issues that enter into the calculus of competitiveness (e.g. "living wage," hazardous job conditions, compensation for workplace injury, and collective bargaining); this aspect of the trade and labour debate will be addressed later in this paper. Of particular concern here are the issues that touch on basic human rights, including non-discrimination in hiring and remuneration (dealt with under International Labour Organization Conventions 100 and 111), child labour (dealt with under ILO Convention 138); and forced labour (dealt with under ILO Conventions 29 and 105).[41]

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[40] The movement for "green GDP" accounting is aimed at improving the situation in this regard. Proponents of the ecological footprint thesis also argue that inadequate biophysical measurement obscures the extent to which technologies that appear to ease pressure on ecologies (e.g. filters or sewage treatment) actually do reduce natural capital input. See Wackernagel et al., op. cit.

[41] See W.A. Dymond, "Trade and Labour," Department of Foreign Affairs and International Trade (mimeo), p. 4. The relevant ILO conventions are from the 1998 Declaration on Fundamental Principles and Rights at Work.

These issues are not directly about trade but rather about policy choices in foreign jurisdictions. Nonetheless, insofar as those policy choices are based on production possibilities enabled by trade, then trade is implicated. This raises the question of the extent to which trade rules can be used to address such issues. In this regard, there are several considerations:[42]

First, using trade remedies to address these issues would result in problems being addressed only in those sectors that are significantly exposed to international trade. Insofar as the issues are manifest in non-export-intensive areas (e.g. child labour is, according to the ILO, little represented in export products), trade measures would have to aim for the overall economy, hitting directly many who are innocent of the targeted practice (and who might have little redress in countries with inadequate distributional frameworks) and probably having negative consequences for poverty.

Second, while the manifestation of the problem is at the industrial level (e.g. child labour in carpet weaving), the objective of trade measures would be to change higher-order domestic policies within the target nation (e.g. public education systems and social policies), not simply to prevent child labour in traded goods. The leverage of trade as an instrument is thus substantially weaker than if the target were simply industrial practices.

Third, trade measures would address the issues in countries whose policies are challenged, leaving similar problems elsewhere not addressed. Given that the poorer and less developed countries, which tend to have the worst labour practices, also trade the least, there would be an inherent tendency for a trade-rules approach to target lesser evils in trading countries while systematically ignoring worse abuses in non-trading countries.

Fourth, since the issue is not product-related but rather process-related, it is linked to the debate over non-product-related processes and production methods (npr-PPMs) in the technical barriers to trade context and faces many of the same technical hurdles in trade disputes.

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[42] This discussion follows for the most part W.A. Dymond, "Trade and Labour," op. cit.

Fifth, the WTO system favours consultation and settlement, rather than rule making. In the event of a settlement, the complaint may be withdrawn, with no formal legal ruling having been made. This could lead to the perverse result that the source of the complaint would remain in force and tolerated as an integral part of WTO rights and obligations. Alternatively, insofar as the sanctioned country chose to tolerate the sanctions (which might be optimal for it if the amount of trade affected were small or could be easily diverted to third markets, an important consideration here since the right to retaliate goes only to the complaining party, and multilateral sanctions are not allowed), WTO remedies would be exhausted without affecting the offensive practice.

Sixth, as a practical matter, most complaints would arise in the United States and European Union and target developing countries, deepening the North-South divide and contributing to geopolitical tensions.

Finally, and not inconsequentially, the trading system would thereby have embedded within it new mechanisms for contingent protection (which, based on experience with other such mechanisms, tend to lead to abuse for protectionist purposes).

These are quite compelling arguments; however, some practical considerations might temper the conclusion to which they lead. For one, to take a page from domestic policy implementation, the tax system is often used to advance policy goals – whether it be to stimulate research and development or to improve child welfare – unrelated to and in fact detrimental to the primary role of the tax system of raising revenue to finance the operations of government. Nonetheless, in a world where policy targets frequently outnumber effective policy instruments, countries make use of such instruments as are in hand.[43] Clearly, use of trade policy in this sense to advance objectives in "trade-related" areas (or "trade-unrelated areas," as Professor Bhagwati pithily calls them) is not necessarily to be excluded, even if on trade policy grounds alone such use would not be recommended. Equally clearly, however, just as extensive use of the tax system has resulted in horrendously complicated tax codes that can leave governments flying blind as to the net policy effects, extensive use of the trade system for non-trade purposes could well result in more harm than good and would be ill advised.

In addition, preparedness to use the WTO or other trade instruments to advance such policy goals can provide an impetus to the revitalization of moribund international institutions that are the more appropriate instrument. This argument has been advanced in connection with the ILO, which, as a result of pressure to incorporate labour standards into the WTO, "is getting significantly more attention, more political support and more resources to deal with core labor standards, especially child labor."[44] It is interesting to note in this regard that in March 2000, the ILO, for the first time in its history, actually used its enforcement mechanism (Article 33) against Myanmar, leading to a rapid response from the authorities of that state.[45]

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[43] Indicative of the enormity of some of the problems with which the international community must in some way cope, at the time when Convention 192 came into force, a child-labour activist group, Global March, reported that there were some 250 million children at work, enslaved or conscripted for prostitution or as soldiers. See "Report Explores Global Spread of Child Labor," available from childhood@globalmarch.org

[44] Kimberly Ann Elliott, "The ILO and Enforcement of Core Labor Standards," *International Economics Policy Briefs*, Institute for International Economics, July 2000: http://207.238.152.36/NEWSLETR/briefs.htm. Elliott notes that the 1999 convention on elimination of the worst forms of child labour (ILO Convention 192) is being ratified at the fastest rate in ILO history. There may be some connection between this sudden alacrity and the increased attention being paid within the WTO to core labour standards. For example, at the first WTO Ministerial in Singapore in December 1996, WTO members renewed their commitment to the observance of internationally recognized core labour standards, while rejecting the use of labour standards for trade protectionist purposes. Subsequently, at the third WTO Ministerial in Seattle in December 1999, a number of proposals were put forward for working groups dealing with the trade and labour issue.

This case raises the question addressed earlier of whether the WTO's teeth are really all that much sharper than what would be possible elsewhere: in the end, as Elliott notes, the WTO leaves it to member governments to take action to remedy violations but does not suspend benefits itself. The ILO's process is not in principle different – and by implication no less potentially effective – if the will is there to use it.

Creating Wealth and Preserving Social Contracts

The second category of trade-related issues consists of those that have distributional or "social contract" aspects. Once the market is adopted as a means of economic organization, there are certain necessary consequences, including the acceptance of inequality in income as a basic fact of life, as well as the need for a social safety net to mitigate the impact of market shifts on individuals. However, insofar as the issues posed by the market turn on the distribution of wealth, they can be addressed, quite literally, by throwing money at them.[46] In other words, no matter how reluctantly and confrontationally, wealth and its distribution can be negotiated in an economic policy setting.

Trade liberalization typically forces domestic adjustment, with winners and losers. The bottom-line results then depend on three key things. First, liberalization must result in an expansion of the overall pie, thereby making Pareto-optimal outcomes feasible (i.e. the polity overall can be made better off with no one being worse off). Second, the internal capacity to deal with the distributional consequences must be in place.[47] And third, the adjustment needs to be fairly rapid since ultimately the legitimacy of liberalization as a policy depends squarely on results.[48]

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[45] Kimberly Ann Elliott, ibid.

[46] This, of course, overstates matters in some important ways, because it is not really possible to reduce all things to dollars and cents. For example, jobs are "ways of life" as well as a source of income, and industrial adjustment sometimes turns whole communities dependent on uncompetitive industries into ghost towns. What's lost is hard to value. Nonetheless, insofar as one can roughly quantify the non-pecuniary benefits of a job as psychic income, the analysis of the issue is not significantly affected.

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[47] Just as risks are less readily managed across borders than within a state, so it is the case that the distributional consequences of structural adjustment to trade pose greater problems than in response to domestic market developments. Within a nation-state, distributional policies and social safety nets to soften the impact of restructuring, downsizing, plant closures and relocations, etc., are at least in principle sustainable because, while some in the nation lose, others gain and, in net terms, the tax base grows through greater economic efficiency. When market forces make allocational decisions across national borders, the situation can be very different because, in the short run, the winners may turn out to be predominantly on one side of the border (or in one grouping of nations sharing similar characteristics), while the losers are on the other side.

On the "winning side" (i.e. the nations that are the short-term net beneficiaries of liberalization), the tax base is boosted and demands on social safety nets reduced, allowing tax rates to be cut. At the same time, exchange rates would tend to be comparatively buoyant, asset markets would improve and interest rates could be lowered compared to where they otherwise would have been. On the other hand, on the "losing side" (i.e. those whose short-term adjustment costs exceed short-term benefits), the tax base is eroded and claims on social safety nets increase; at the same time, in a context of mobile capital, there may be reluctance to raise tax rates. These pressures can be further intensified by downward pressures on exchange rates and asset values and upward pressures on interest rates.

Meanwhile, the internal tensions within the society on the losing side would likely be exacerbated if liberalization changes the permeability of borders to different factors of production to different degrees and, as tends to be the case, capital is made relatively more mobile compared to labour, and skilled labour made comparatively more mobile compared to unskilled labour. In such circumstances, disparities in income distribution widen within economies. In a similar vein, increased job turnover due to restructuring leaves many workers with lower-paying jobs, notwithstanding the fact that, overall, the job structure might, because of the increased trade, shift toward more productive and higher-paying jobs.

[48] Robert Keohane and Joseph Nye present a cogent argument that the legitimacy of the trade system rests on its results rather than on its "democratic" procedures. What has created a problem of legitimacy for the

Unfortunately, economic theory offers no insight into how fast the adjustment will be, nor how deep a structural adjustment downturn may be. This underscores why states do not enter lightly into trade and/or investment liberalization agreements – the prospective gains have to be quite significant to warrant undertaking the various risks and burdens of change.

Canada's experience in this regard is examined by Philippe Massé in his contribution to the GCON Working Group on World Trade Issues.[49] Based on his literature review, Massé concludes that, viewed over a long period, trade appears to have contributed positively to employment growth in Canada, but has led to job losses in mostly low-technology, labour-intensive sectors that employ large numbers of low-skilled workers. Also of importance, the paper highlights that turnover in the labour market is very high, and in fact much larger than the effects that could be attributed to trade liberalization.

As regards the impact on wages, the paper concludes that the widening wage differentials observed in Canada reflect principally structural trends in terms of the demographics of the labour force and institutional structures and cannot be attributed either to trade or to technological change, although the shift in demand toward higher-skilled workers is due more to technology than to trade.

Since effective labour market policies are required to facilitate market adjustments due to technological and demographic change, there is not a strong reason to curtail trade and investment or to slow liberalization on social contract

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international system in recent years, they suggest, is a lack of effectiveness. For example, the attack on the IMF in recent years derives in good measure from its lack of effectiveness in the Asian Crisis; by contrast, WHO got credit for eradicating smallpox (although its weak response on AIDS is eroding that credibility). See R. Keohane and J. Nye, "The Club Model of Multilateral Cooperation and the WTO: Problems of Democratic Legitimacy," paper presented at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Center for Business and Government, Harvard University, June 1-2, 2000.

[49] See P. Massé, "Trade, Employment and Wages: A Review of the Literature," in *Trade Policy Research 2001*, op. cit.

grounds. In short, trade policy can in effect "free ride" on what is in any event an institutional requirement for any economy that buys into the market system in the first place.

Economic and Technical Regulation

The third class of domestic regulation identified earlier is that of economic and technical regulation. While in principle it should be easier to square domestic economic regulation with international rules, since governments should generally be indifferent to questions of how efficient outcomes are to be achieved, this is not actually the case because of the differences in initial conditions across jurisdictions, coupled with the general "second best" difficulties posed by sub-optimality being the rule rather than the exception.

Against this background, it is useful to take a look at one of the more controversial examples of the intrusion of international rules into domestic policy space to see if some lessons can be extracted as to how to deal more generally with the evidently broad range of such intrusions. TRIPS is a good test case in this regard because it is more or less purely economic regulation and might be considered the "pawn to king four" move in launching the implementation of the new trade policy agenda. Of particular interest here are the criticisms that are of a technical nature. In this regard, TRIPS has been criticized on:

- economic and technical grounds for:
    - creation of rents in excess of what would be optimal in terms of stimulating innovation;[50] and

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[50] Intellectual property is a complex issue; there is an open debate about how much protection is required to provide the incentives for research and development that stimulates innovation. For example, the role of tacit knowledge is viewed by some analysts as a very significant factor conditioning the ability to actually use formal knowledge (or "template knowledge," which is readily copied), which affords intellectual property a good measure of protection even without regulations. See, for example, R.N. Langlois, "Knowledge, Absorptive Capability, and Organizations," *1998 APEC Economic Outlook Symposium* (APEC Secretariat, Singapore:

    - the very choice of rent creation through granting of monopoly rights in lieu of alternative forms of intellectual property right protection, a choice that *inter alia* introduces constraints on competition into international law;
- more general economic welfare grounds for one-sided protection of producer rights without corresponding consideration of consumer rights;
- legal grounds (potentially undermining rights provided by World Intellectual Property Organization conventions to individuals to directly press their rights in domestic courts); and
- process grounds because TRIPS locks in a particular substantive regime that will be very hard to adjust given the requirement for consensus.

The question that these critiques raise is whether it is reasonable to expect a sound economic regulatory framework, in terms of choice and design of instruments, to emerge through international negotiations, at least insofar as these negotiations aim for positive regulatory outcomes? Second, even if an optimal regime could be so negotiated, is it wise to entrench any particular regime in a difficult-to-change international accord when changing conditions might warrant modifications from time to time?[51]

1998): 67-73. Moreover, the optimal amount of protection is thought to vary widely by industry. In some cases, technology can be readily reproduced through reverse engineering or the technology is embodied in an easily copied product (e.g. a bio-engineered grain that can be simply grown in order to obtain boundless copies). But this is not a uniform condition facing all industries.

[51] This has already become a practical concern, given developments in biotechnology, in view of TRIPS provisions that provide scope to exclude certain biological discoveries. TRIPS is controversial in a number of other ways. While a full discussion would be a digression, the issues are worth passing mention. First, some see TRIPS as anomalous in the multilateral framework since it did not entail an exchange of benefits between WTO members but rather a transfer of income from developing to developed countries (for an interesting game-theoretic estimate of the losses to developing countries that resulted from the asymmetric move to symmetric

This issue is complicated to some extent by the fact that much of the substantive force of TRIPS comes from its incorporation of existing substantive international agreements such as the Berne, Rome and Paris Conventions. However, it does incorporate substantive provisions of its own.[52] Moreover, the above critiques stand even for indirect incorporation of substantive measures, if the latter were agreed under a different implementation regime than TRIPS.

However, by embedding substantive regulation in the framework of multilateral rules, the Uruguay Round started to

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levels of final protection, in contrast to GATT practice vis-à-vis tariffs of symmetric moves resulting in asymmetric levels of final protection, see J.D. Gaisford and R.S. Richardson, "The TRIPS Disagreement: Should GATT Traditions Have Been Abandoned?" *The Estey Centre Journal of International Law and Trade Policy*, Vol. 1, No. 2, 2000, pp. 137-170. This discussion nonetheless underscores the core commercial nature of the agreement, and one may equally ask why it is not legitimate to trade one commercial consideration for another of a different type? Moreover, developing countries did obtain some benefits, as is shown by India's recent move to extract royalties from Western pharmaceutical companies for use of plant remedies that originated in Indian folk medicine (see "The Trade Agenda," *The Economist*, November 11, 2000, p. 83). Given that tropical countries are host to the large majority of the globe's species, this provides developing countries with significant opportunities they may not have anticipated at the time of the Uruguay Round (see S. Ostry, "The Uruguay Round North-South Grand Bargain," paper presented at the conference *The Political Economy of International Trade Law*, University of Minnesota, September 15-16, 2000, p. 21). Moreover, insofar as some innovation in at least some developed countries is stimulated, some spillovers will accrue in the developing world. Implementing intellectual property protection also removed some impediments to imports by developing countries of goods embodying advanced technology and foreign direct investment in areas susceptible to piracy, generating additional economic benefits (e.g. see P.J. Smith, "Are Patents a Barrier to U.S. Exports?" *Journal of International Economics*, Vol. 48, No. 1, pp. 151-178). Furthermore, TRIPS added an important "arrow to the quiver" of developing countries in pressing retaliation against developed countries (e.g. the EU Bananas – Ecuador arbitration panel affirmed that withdrawal of TRIPS-based concessions is feasible).

[52] For example, the TRIPS Agreement specifies the protection that computer programs are to be afforded.

restrict the flexibility that GATT principles afforded domestic policy, namely that policy measures were subject only to the overriding principles of non-discrimination among trading partners and the use of the least trade restrictive measure required to achieve domestic policy objectives.

Finally, TRIPS includes a provision that is hard to justify given the discussion in this paper: under Article 8, TRIPS requires that even "measures necessary to protect public health and nutrition and to promote the public interest in sectors of vital importance to their socio-economic and technological development" must be consistent with the provisions of TRIPS – in other words, vital socio-economic objectives must defer to TRIPS objectives if there is a conflict in implementation.[53]

The bottom line, however, is that at the end of the year 2000, some 70 countries have yet to implement TRIPS commitments, discussion of implementation problems have failed to identify workable solutions, pressure for a fundamental re-evaluation is growing as new issues pile on, and important ad hoc adjustments (by pharmaceutical companies regarding essential medicines) have already had to be made.

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[53] In this regard, TRIPs has been attacked on moral grounds for contributing to the human tragedy of AIDS in poor countries due to prevention of compulsory licensing of life-saving drugs. It is an interesting question how countries will react to a policy conflict of this nature. Redress for violation of TRIPS would require some jurisdictions – presumably the United States and/or European Union – to launch a complaint in the WTO. The politics of this would, in this type of situation, weigh against a complaint being launched in the first place (indeed, the U.S. has moved to deal with the problems posed by its intellectual property laws for sub-Saharan African countries seeking affordable access to AIDS drugs – see discussion in J. Vellinga, op. cit.). If a complaint were launched, the situation of the developing country would likely find considerable sympathy within the WTO. Even if some retaliation were authorized, such retaliation would have to pass through democratic procedures in the U.S. and the EU, where again a political gauntlet would have to be run. Even in the highly unlikely case that some retaliation were actually implemented, the developing country could simply suffer it, as the EU is suffering retaliation in the beef hormones case, while focussing on diverting its affected exports to third markets; given that developing-countries' exports tend to have high cross-price elasticities of demand, this would not be overly difficult. In short, there seems to be an open invitation to non-compliance in this element of TRIPS, which points to a flaw in its design.

Conclusions and Future Directions

While the foregoing discussion amply testifies to the complexity of the issues, some conclusions can be teased out.

First, the trade-related "values" issues are not uniformly about domestic policy space; some are, including trade and health, trade and culture and aspects of trade and environment. Some, however, are about foreign policy (i.e. they concern circumstances and practices in foreign jurisdictions). These include the trade and core labour standards issue and trade and global environment issues.

In the past, the WTO's dispute settlement system has tended to avoid pronouncing on the merits of the substantive domestic policy issue implicated in a trade case, preferring to rule only on whether the means to the desired end was WTO-consistent. Moreover, it has not supported extraterritorial application of domestic policies.

These tendencies cut two ways. They help protect domestic policies from the reach of trade policies, provided they are implemented in a non-discriminatory manner, an issue of design not substance. At the same time, they make trade rules an ineffective means to get at policy objectives that are broader than trade transactions, particularly in an extraterritorial way in foreign jurisdictions.

Second, the capacity to manage risk across borders is lower than within a state. This suggests that the capacity to expand trade in areas where risk is an important factor will lag the expansion of the role of the market within borders. A corollary of this is that, while trade policy can legitimately be expected to open up markets where they exist, it probably should not be used to create markets where they do not exist, since this risks pushing societies faster and further than their internal frameworks for managing market-related issues can cope with.

Third, the "values" issues tend to involve public goods that are in some sense "non-negotiable" or, put another way, that are equal to or have primacy over the pursuit of wealth. These include health (physical life), culture (socio-cultural life) and environment (ecological life).

In a domestic setting, government policies constrain the reach of the market insofar as it is deemed necessary or convenient to balance the attainment of objectives in these areas versus giving rein to the pursuit of wealth. In an international context, there is some sentiment in the literature that this should be the case as well, that trade rules should show what might be termed "substantial deference" to domestic preferences in the case of issues where the idea of market-determined outcomes collides with deep ethical, social and political principles and values.[54]

Some change to the body of WTO law would seem to be required. For example, the TRIPS provision that gives precedence to intellectual property interests over vital socio-economic objectives if there is a conflict in implementation would seem to need reconsideration (not least because it has already had to be de facto reversed in the case of AIDS medicines for hard-hit nations). The difficulty of giving some deference to cultural concerns under the present formulation of Article XX (which requires that a measure be required for compliance with another WTO-consistent law to provide grounds for an exception) also suggests that Article XX needs some amendment. And the WTO's Dispute Settlement Body through exercise of essentially political judgement should attempt to steer the application of WTO law in such a way as to minimize system friction.[55]

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[54] The term "substantial deference" is borrowed from Michael Trebilcock and Julie Soloway's article "International Trade Policy and Domestic Food Safety Regulation: The Case for Substantial Deference by the WTO Dispute Settlement Body under the SPS Agreement," presented at the conference *The Political Economy of International Trade Law,* University of Minnesota, September 15-16, 2000.

[55] For a detailed discussion of how it might be made to work in the SPS context, see M. Trebilcock and J. Soloway, op. cit. The rather adroit fashion

Fourth, reflecting the inevitability of eventually declining returns to more wealth, coupled with high positive income elasticities for "quality of life" factors such as health, richness of culture and a clean environment, the comparatively wealthy industrialized economies and comparatively income-poor developing economies will naturally have different preference structures. This suggests a two-speed WTO for inclusion of trade-related "values" issues.

Fifth, buying into the market economy necessitates development of social contracts, broadly writ, to control the risks to individuals. Extending the division of labour from a national basis to an international or global basis through trade and investment neither diminishes this need nor expands it. And in the present context of "thick" borders, it would appear safe to conclude that trade and investment does not compromise the ability of nation-states to preserve social contracts. The quid pro quo for obtaining the gains from trade would appear to be substantial deference to trade rules, even where they reach inside the border (something which appears inevitable and increasingly likely) and even where they necessitate

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in which the WTO sorted out the *Shrimp-Turtle* case lends some encouragement that the WTO can show political sensitivity and what at least some observers consider proper deference to the underlying environmental concern. In particular, the case has been made that the preambular references to sustainable development in the WTO Act served an important role in guiding the Panel and Appellate Body decisions. This point is made by W.A. Dymond, "Environment and Trade: Lessons of the MAI," op. cit. At the same time, there is the overriding question of whether the dispute settlement system could bear the weight that this approach would put on it. Showing deference means applying judgement, which in these kinds of cases necessarily would involve judgements about the merits of the substantive issue implicated in a trade dispute. Rather than lowering the temperature, however, this might take the WTO from the frying pan directly into the fire. This suggests that the scope for dealing with these issues through judicial activism by the Dispute Settlement Body is very limited and formal agreements will have to be reached on each of the sensitive issues. While this can probably be done only in the context of a round, and therefore is likely to be some way off in the future, the light case load in this area provides some comfort concerning the possible erosion of domestic policies.

compensatory adjustments to domestic social contracts. In short, there is no reason why trade policy cannot in effect "free ride" on what is in any event an institutional requirement for any economy that buys into the market system in the first place.

Sixth, establishment of substantive technical regulation at the international level through a trade negotiation process, where shorter-term commercial considerations could well compromise the efficiency of the rules, does not appear to be a good idea. Even incorporation of substantive measures from other international agreements is subject to question if the implementation context in which those agreements were developed (not to mention the composition of the community that negotiated those agreements and/or joined voluntarily) differs from the WTO's. Generally, this suggests that WTO instruments should emphasize procedural rules, as does for example the Agreement on Sanitary and Phytosanitary Measures (SPS). At the same time, it suggests that instruments should avoid building substantive rules into the body of hard-to-change WTO law, as done by the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

Future directions

Trade policy (at least in its "legislative" sense, meaning multilateral negotiations for liberalization and further rule amendment or development) is currently in hiatus. By some estimates, this hiatus may be quite lengthy – especially if the terms of China's accession leave that country constrained in terms of offers for further liberalization in the short term, and if the European Union eventually finds that it needs to resolve its agricultural policies with respect to prospective entrants before, rather than in conjunction with, a new round. Accordingly, there may well be some time to develop a grand architecture of rules and/or relationships between various rule regimes to resolve the issues discussed above. At the same time, it is quite possible that determination of such a grand architecture may prove impossible, if the inconclusive nature of the "coherence" discussions is any guide.

In the meantime, the WTO does not stand still. This reflects the fact that accession negotiations continue and the dispute settlement mechanism continues to function. The decisions and interpretations generated by the latter activity help not only to keep trade flowing by greasing the system, but also to fill in gaps and clarify murky passages in the legal framework of the WTO and to develop an information base that will support the next round of negotiations.

Accordingly, a lengthy hiatus in negotiations may yet be the optimal result for the WTO – and would not necessarily imply a hiatus in development of the multilateral framework. This is particularly the case because, as this survey has shown, the multilateral system is at a crossroads of sorts and careful thought about future directions is required.

Trade and Civil Society: Toward Greater Transparency in the Policy Process

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Introduction

The involvement of civil society organizations (CSOs)[1] in the trade policy process has become perhaps *the* central issue in the lively and often acrimonious debate on the "democratic deficit" held by many to exist in the functioning of the multilateral trade system. Critics of the trade system and its crown jewel, the World

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[1] The term "civil society" is both very old and very new. For the purposes of this paper, civil society organizations are considered very broadly to include groups of people claiming to represent perspectives on particular public policy issues.

Trade Organization (WTO), see such a deficit in the process of trade negotiations, in the administration of the system and, perhaps even more importantly, in the functioning of the WTO's Dispute Settlement Body, which in its first five years of existence is evolving into a serious pretender to the status of Supreme Court for the global economy.

This view not only persists but also appears to be gaining increasing currency, despite the unprecedented degree of consultation, transparency and openness evidenced in many countries (and especially in Canada) in the preparations for the abortive attempt to launch multilateral negotiations that ended in such disarray in Seattle in December 1999.

That Seattle marked the end of the "traditional" process of trade negotiations and administration of the multilateral trade system – which to many is little differentiated from the management of globalization itself – is disputed by virtually no one these days. The question is how, and by how much, to change: who to bring into the process, in what manner and subject to what constraints? That civil society, broadly writ, is to be part of the "who" is not in serious doubt. However, the nature and scope of CSO involvement is both complicated and highly sensitive. CSOs also differ amongst themselves and number in the tens of thousands; no easy formula to accommodate their participation is in hand. Domestic policy formulation processes differ widely from one WTO member economy to another – no organizational model is the right one, or acceptable to all. More importantly, there is the question of how much real influence over the outcome of negotiations or administrative decisions could or would be allowed by governments who comprise the membership of the WTO.

This paper takes up the question of what would be appropriate means to bring CSOs into the trade policy process in light of the developments that have brought the multilateral system to its current governance impasse, and of the new complexities that lie ahead – in terms of emerging new issues, a changing context and, last but not least, in terms of prospective new members, most importantly China.

How We Got to Where We Are: The Road Map Looking Backwards

Some – and arguably the most significant – of the reasons behind the increasing involvement of civil society with the multilateral trade system can be summarized in the following stylized facts describing the evolution of the trade system and the globalization of the economy, which trade and investment at once contributes to, epitomizes, and is powered by.

Trade has become too important to be left to the elites

The rise in the importance of international trade since the Second World War is well known; however, its true extent and penetration into every society in every part of the world is rarely fully appreciated. The value of merchandise exports as a share of global GDP rose from about 7 percent in the early post-war period to around 25 percent by the close of the 20th century. At the same time, the more difficult to measure cross-border trade in services rose from a negligible percentage of global GDP to about 7 percent.

However, these statistics, dramatic as they may be, tell only part of the story. The growth of foreign direct investment has been such that the value of sales by foreign affiliates of multinational companies now is thought to be roughly equal to cross-border trade in the case of merchandise and is well over one and one half times larger than the value of cross-border trade in services.[2]

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[2] As is recognized in the General Agreement on Trade in Services (GATS), sales through foreign affiliates ("commercial presence") is one of the modes of trade in services. Adding sales through commercial presence to cross-border sales thus gives a truer picture of the extent of services trade. Although it is not

Adding together exports of goods and services on a cross-border basis with sales through commercial presence, total "exports" in this broader sense would appear to be equivalent to two thirds of current global GDP. Imports, of course, account for a similar share of global GDP, emphasizing the extent to which trade has penetrated the pith and substance of economic activity worldwide.

These last statistics are rarely cited, yet their significance is felt deeply within societies. With the rise in the significance of trade and investment for economic growth and development around the world, public willingness to leave trade policy exclusively in the hands either of the politicians or of their trade policy experts appears to have begun to dissipate.

The trading system is probably not an exception in the sense of having long been managed by elites but coming under closer scrutiny more recently. As Robert Keohane and Joseph Nye point out, the General Agreement on Tariffs and Trade (GATT) fit well into the post-war international economic regime, which they describe in terms of a club model where each minister had his or her own international "club," dealing with its own cluster of

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commonly done, one can do the same calculation for merchandize trade. This not only gives a better appreciation of the penetration that goods and services of foreign provenance have made into domestic economies, but also provides a summary statistic that encompasses both trade and investment flows, an important consideration given the fact that trade is "one-off," whereas investment cumulates over the years and generates a growing volume of sales. A few caveats are in order, however, with respect to this calculation. First, a large share of recent foreign direct investment has been in the form of cross-border mergers. In such instances, the ownership of the firm may change but there is no foreign content necessarily introduced into the goods or services produced by the firm. Second, with the fragmentation of production by multinational corporations across borders and the associated rise of intra-firm trade, the growth of trade in terms of gross flows has exceeded the growth of value-added generated through trade. While these developments have muddied the interpretation of trade statistics, the point remains that international commerce, broadly interpreted, considerably exceeds trade as measured by cross-border transactions alone.

issues, where international bargains could be struck involving either traditional international law or agreed practices ("soft law"), without close links to other issue areas. The club model kept outsiders out (including officials in other ministries within one's own government) and insulated ministers from domestic pressures, making it easier to work out agreements. Lack of transparency was thus purposeful and a means of reducing the cost of negotiations.[3]

The collapse of this "club model" more generally may also have been part of a larger social phenomenon. Sylvia Ostry has argued that the growth in citizen engagement "reflects a broader and more pervasive secular change in the industrialized countries – an alienation from the elite." As she notes (citing the work of American sociologist V.O. Key, Jr.), a "permissive consensus" existed for several decades following World War II: the general public supported the government's foreign policy, including trade policy, while knowing little about the details. This left governments free to sort out issues as they saw fit or expedient. Ostry points out: "The deference to government, and more broadly to the establishment as it was then termed, underlay the permissive consensus and has dramatically declined since the 1960's in all OECD countries as many recent analyses of opinion polls have demonstrated. Perhaps the Uruguay Round was the last gasp of the permissive consensus – and barely that."[4]

While the changes appeared to be quite dramatic in the 1990s, with hindsight it can be seen that the seeds were planted long ago. Over the decades, the policy process had been progressively opened up to a wider range of interested parties in many countries around the world. While business representatives in many countries had been consulted on trade policy matters regularly or on an ad hoc basis from the 1950s onwards, over time the list broadened to include labour unions, small and medium-sized enterprises, public interest advocacy or citizen action/human rights groups, and consumer groups, never mind environmental associations – whether at the behest of governments looking for advice or analysis, in response to demands of the non-governmental groups to be heard, or in the interest of forging partnerships to implement agendas.[5]

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[3] See R. Keohane and J. Nye, "The Club Model of Multilateral Cooperation and the WTO: Problems of Democratic Legitimacy," paper delivered at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium,* Center for Business and Government, Harvard University, June 1-2, 2000.

[4] See S. Ostry, "WTO: Institutional Design for Better Governance," paper delivered at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium,* Center for Business and Government, Harvard University, June 1-2, 2000.

Meanwhile, interest in trade matters within the general public also rose, stoked by – and in turn feeding – close media attention that raised the level of rhetoric, if not the level of understanding.[6] It has been some years since trade policy was shaped exclusively by technocratic advisors to governments and negotiated in a clubby atmosphere shielded from public scrutiny by diplomatic confidentiality. Such a circumstance is unlikely to emerge again.

Trade policy stepped "outside the box," treading tentatively but carrying a very big stick

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[5] The involvement of CSOs in consultations obviously varies widely from jurisdiction to jurisdiction. Canada has long had policies on citizen participation in the policy process, ranging from outreach by civil servants to appearances by individuals and organizations before parliamentary committees. A high point for partnership between government and civil society was of course in the advancement of the ban on landmines, led by Foreign Affairs Minister Lloyd Axworthy and a range of activist civil society organizations that had international reach and substantial financial and human resources of their own.

[6] Sylvia Ostry suggests that the general lack of interest by the general public in trade negotiations persisted up to and included the Uruguay Round. As she puts it: "There was very little public interest in the Uruguay Round negotiations. As the new Director-General of the WTO, Mike Moore, has described it: 'The Uruguay Round was launched in the silence of public apathy.' The same could be said about the previous seven rounds since the creation of the GATT in 1948." See S. Ostry, "WTO: Institutional Design for Better Governance," op. cit.

Not only trade but also trade policy became increasingly more important over the years, for several reasons. First, as the share of global production that was traded grew, the character of the global economy evolved from what has been termed a model of "shallow integration" to a model of "deeper integration."

Second, the triumph of the market model, marked symbolically by the fall of the Berlin Wall in November 1989 (which culminated a period of change in regimes in much of Latin America, Africa and Asia), led to its application with increasing assuredness in many areas where considerations other than efficiency clamoured for attention.[7] Trade, being the leading "spear carrier" for market economics – as indeed it has been since the days of Adam Smith, David Ricardo and others who wrote the early economics largely as a defence of free trade[8] – bears, along with the IMF and the World Bank, the brunt of reaction – and there is no point in trying to duck this.

Third, and quite inevitably given the expansion of the share of trade in overall economic activity, trade policy began quite self-consciously to reach inside the border – which is the same as saying that it "stepped out" of its traditional "box" of reducing the level of barriers to trade at the border.[9]

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[7] Three areas in particular stand out: health, culture and the environment. Societies have broadly reconciled themselves to living with inequalities of income in order to realize the efficiency benefits from applying the calculus of markets to economic production; they are not so inclined to accept the application of the market calculus to life itself – whether it be physical, social or ecological. The issue is not trade per se, but the growing weight of market economics in areas where efficiency must be traded off against other values.

[8] See W.W. Rostow, *Theorists of Economic Growth from David Hume to the Present*, Oxford University Press, 1990, p. 78.

[9] The following passage is representative of the reaction that the intrusion of trade rules inside the border has elicited: "Although still a little-known and little-understood institution, the WTO has become increasingly controversial as it has expanded the scope of its work from its original narrow GATT focus on reducing tariffs on manufactured goods. The WTO now also works to eliminate nontariff barriers, and can be used to challenge environmental, health, and other

The strengthening of enforcement powers through the creation of the Dispute Settlement Body (DSB) in the WTO had arguably even greater potential significance. In what is now going on seven years, the DSB has handled more than twice as many disputes as came before the GATT in close to half a century before that.[10] Moreover, it has been ruling on issues that touch profound social and cultural sensitivities: for Canada, these have included rulings on milk marketing boards and cultural policies on magazines; other rulings have touched on flashpoints such as trade in genetically modified foods and potential health hazards such as asbestos, on fisheries practices that endanger dolphins and turtles, and so on. The DSB has effectively been evolving into the equivalent of a global Supreme Court, ruling on a wide range of sensitive socio-economic issues. And, in a context where negative consensus rules the day (i.e. *every single WTO member* has to agree to overturn a decision), and where trade retaliation running into the billions of dollars can be unleashed to enforce its decisions, it is a very powerful Supreme Court at that.

Finally, in North America at least, NAFTA's Chapter 11 protection for investors has given some groups within societies – in this case foreign investors, who are actually "outsiders" in a national social context – the right to challenge in court decisions by democratically elected governments. CSOs might not consider

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regulations that may serve legitimate social goals but may be regarded as impediments to international trade. The 1995 replacement of GATT by the WTO heightened concern among critics because its stronger enforcement powers represent a further shift in power from citizens and national governments to a global authority run by unelected bureaucrats. Business, academic, and government supporters applaud the WTO as a more muscular sheriff of the world trading system." See S. Anderson and J. Cavanagh, "In Focus: World Trade Organization," *Foreign Policy in Focus*, Vol. 2, No. 14 (Institute for Policy Studies, January 1997), available at http://www.foreignpolicy-infocus.org/briefs

[10] In large part, the growth in the number of cases reflects the expansion of the volume of global trade and the growth in the number of members of the WTO, rather than a rise in litigiousness, as sometimes has been argued. This observation is due to Marc Busch, Queen's University, Kingston, Ontario.

this a right "to die for" but certainly "to very vocally demonstrate for."

Thus, at a time when the widening application of market instruments and the in-reach of trade policy are creating tensions both within and among trading partners over domestic norms and the social institutions that embody them (which are also issues of great concern to civil society), trade policy institutions have acquired powerful leverage over these very same issues. It should come as no surprise that CSOs want "in" to trade policy – and not merely to be listened to and politely shown the door when the time comes for serious decision making.

Globalization changed the terms of the social bargain

At least in developed countries, globalization is making it increasingly difficult for governments to carry out some of their traditional social policy functions. In particular, the services of larger and larger segments of the working population are becoming more easily substitutable across national boundaries, resulting in increasingly difficult challenges in national labour markets.

At the same time, the competitive pressures on national economic systems from international trade directly constrain tax policy choices, while the debt burden arising from fiscal excesses in earlier decades continues to limit discretionary and program spending. Accordingly, the economic and fiscal bases for the balancing act between the interests of labour and capital that formed the basis of the post-war political economy have felt an impact – and precisely at a time when globalization has dealt a distinctly better hand to capital than to labour.

Given the evidence that international borders still matter, as the recent work of John McCallum and John Helliwell shows,[11] it is debatable how significant the impact has been (and how much of it can be legitimately attributed to globalization as opposed to other factors, such as technological change). However, whatever the facts may be, the impression has been broadly implanted that globalization has changed the terms of the social bargain in many countries and to varying degrees. Some CSOs have sensed this and have been rushing into what they see as at least a partial vacuum to influence, shape and/or replace some of governments' activities in administering the social contract. What they are clearly seeking is to *rebalance*, not simply to be heard.

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[11] See, for example, J.F. Helliwell, *Globalization: Myths, Fact and Consequences*, Benefactors Lecture, 2000, C.D. Howe Institute, October 2000.

Disparities widened

Related to the preceding factor, public discussion of open markets and of trade has increasingly centred on issues of fairness and of justice. An important, if not the main, driver for this debate has been the stunning emergence of nearly unimaginable tech-created wealth, co-existing with utter poverty in one and the same economy, at one and the same time, and because of one and the same underlying cause: market-driven economic principles as exemplified in its pre-eminent institutions, the stock market and the multilateral system of trade. The fact that, in many cases, this wealth has come into existence virtually overnight through financial market voracity for technology-related stocks floated in initial public offerings (IPOs), if anything accentuates the sense of unfairness (at least among those who missed the IPO boat!).

Thus, what many see as the success of more open markets and of better international trade rules,[12] others in our societies see as an irreversible march down a road toward ever-wider inequalities. This is something that they do not understand and something over which they sense they have little control. To some extent, this has fuelled the emergence of the CSO movement as a politically relevant social structure that responds to these issues.

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[12] What is perhaps even more interesting to note is that there is nothing in the theory of market economics that would ever predict the widening of income disparities that has characterized the most recent decade. Indeed, the Stolper-Samuelson variant of the main theory of international trade would suggest that we should have seen factor-price equalization – not only between the same factors in different economies but, given that capital is nothing other than transformed labour, also between different factors such as capital and labour in

In an ever more complex world, CSO expertise is needed

As the world economy became more complex over the past decade, governments in many countries were downsizing, particularly their policy analysis and development capacity. Thus, even as the amount of information was growing exponentially, governments were reducing their capacity to absorb and understand it.

Many CSOs represent the self-organization of individuals with keen interests in particular areas; they possess, therefore, a reservoir of knowledge, skills and perspective that could be deployed to great advantage for policy development. This includes information that bears on the gamut of trade policy issues, from negotiations to administration of the multilateral system to the effective disposition of trade disputes.

The effect of these recent and important developments is that, overall, governments have lost ground to some CSOs (as well as other organizations) in knowledge management. In short, many CSOs have become players because, in an information age, they possess information and the expertise to manage and deploy it.

Network technology empowered...networks

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one and the same economy. The fact that this has not happened has not deterred triumphalism in market economics – although clearly it should have tempered it.

It has been argued that the economic basis for the existence of firms was informational efficiency.[13] This idea extends quite readily and naturally to any large, hierarchical organization, including much of the bureaucracy that supports public governance.

Horizontal networks are an alternative form for information management. Indeed, the dramatic decline in the cost of maintaining networks through the information and communications technology revolution has equally dramatically changed the competitive conditions between hierarchical organizations and horizontal networks, in favour of the latter.

Many of the descriptions of the "organization" of the protests in Seattle and Washington drew on military concepts of mobilization and co-ordination to explain the effectiveness of CSOs. However, their effectiveness was not based on traditional informational advantages of large hierarchical organizations; rather, it was based on the effectiveness in self-organization of large numbers of individuals and groups loosely linked in largely horizontal networks or what might be termed "swarms."[14]

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[13] See R.H. Coase, "The Nature of the Firm," *Economica*, November 1937, pp. 386-405.

[14] Kevin Kelly, Executive Editor of *Wired* magazine, describes the advantages of "swarm systems" in terms of (a) their adaptability to a wide range of conditions; (b) their evolvability; (c) their resilience, which is based on multiple redundancies, which in turn means that failure of any one individual component in the system does not matter in particular; (d) their boundlessness, as positive feedback creates new structure – "a swarm can build its own scaffolding to build further structure"; and (e) their ability to generate novelty, which rests to an important extent on the combinatorially large number of possible connections of individuals or ideas within the system. At the same time, he describes swarms' negative features in terms of their being: (a) non-optimal in terms of efficiency (due to the same redundancy that makes them resilient); (b) non-controllable, because there is no authority in charge; (c) non-predictable, which is the flip side of novelty; (d) non-understandable, in the sense that outcomes of swarm behaviour cannot be traced linearly to particular causes; and (e) non-immediate, in the sense that it is not possible to mobilize the system at the flip of a switch (which is the strength of command and control

That network technology empowers networks is of course almost tautological. CSOs are able to share both substantive and tactical information and analysis with like-minded groups all over the world. They represent a new organizing principle for issue management. And this is largely built on technology.

"First we take Manhattan...": from Paris to Seattle to Washington

Leonard Cohen's counterculture anthem could have been written for the CSOs – if he had got the cities right. But the road ran not from Manhattan to Berlin, but rather from Paris, where CSOs celebrated the demise of the OECD-led negotiations for a Multilateral Agreement on Investment (a demise that in the estimation of many within the CSO ranks they also brought about); to Seattle, where organized CSO opposition stole the media show, materially delayed the proceedings and sapped political will when it was badly needed to overcome the deep substantive divides within the ranks of WTO members; and on to Washington four months later, where the World Bank/IMF meetings were the target.

There was a sense among some CSOs of increased confidence resulting from their perceived role in causing or precipitating the failure of negotiations under the auspices of the OECD between 1995 and 1998. That confidence has now soared in the wake of Seattle and Washington (and Prague, and Windsor, Ontario).

Many CSOs seem to believe that the business-directed agenda of the 1980s and early 1990s was successfully deflected by them and should continue to be so. Quebec City will be the next test for governments, CSOs, the media and others.

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hierarchical systems). See K. Kelly, *Out of Control*, Addison-Wesley Publishing Company, 1994, pp. 22-24.

Political economy revolves around the nation-state, but who speaks for the global commons?

Finally, although circumstances continue to change, the fundamental organizing principle of the world's population (dating from the Treaty of Westphalia in 1648) and of the world economy remains the nation-state. While there has been much talk of the demise of this institution, as noted earlier, recent research suggests that this conclusion was premature: borders still matter very much and the nation-state remains very much in business.

The WTO is a creation of nation states; it is an intergovernmental instrument that is central to the governance of the international trade system. And Seattle notwithstanding, it is also one of the most successful of the international institutions – if not *the* most successful.

While the resources directly available to the WTO are not particularly large, the intellectual capital that supports it is huge. Most of this intellectual capital lies not within governments but in the extended trade policy intelligentsia scattered around think tanks and universities worldwide – and, as well, increasingly within the legal community, which is finding trade policy of growing interest due to the new-found litigiousness of the trade system, and which brings to the issues its own set of normative perspectives and its own technical tool kit.

The WTO thus has its own confident and resourceful supporters, who do not necessarily see the CSO "swarm" as intellectually on their own plane or worthy of participation in the high temple of capitalism.[15]

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[15] In this regard, see M.J. Trebilcock, "Mostly Smoke and Mirrors: NGOs and the WTO," mimeo, U.S. Library of Congress and New York University Law School Conference, New York University Law School, March 10, 2000. Professor Trebilcock admits to the polemical nature of this otherwise scholarly article, having, as he puts it, "abandon[ed] the detachment of the Academy for the passions of the Acropolis." With the increasingly polemical nature of the dialogue between CSOs and trade policy practitioners, one senses that an "us versus them" attitude is becoming entrenched.

At the same time, while governments clearly speak for matters within their borders, and in democracies carry the additional authority conveyed by the fact that they also speak for the people within their borders,[16] there is an open question of "who speaks for the global commons?" Global institutions have, of course, been set up by governments to deal with these issues; however, there is increasing evidence that the ball is being dropped on global commons issues – whether it be with respect to migratory fish stocks, the ozone layer, pollution of the most remote ecosystems, global warming or biodiversity and extinction of species (which can scarcely be viewed in national terms, even though all land-based biological species fall within one nation-state or another).[17] In a world where legitimacy is ultimately conveyed by performance, the inadequacy of the intergovernmental institutions in defending the global commons has arguably made this area contestable. Insofar as CSOs self-select to defend the global commons, and provide a compelling case in the court of public opinion as to their commitment and understanding of the issues, the issue of "who do they represent?" at least in this narrow sense seems to fall away. Accordingly, with global commons issues intensifying, the stage would appear to be set for an escalation of the conflict.

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[16] This point has been the basis for the sharpness of the reaction within many governments to the CSO pressure for some form of participation. A recent detailed articulation of this view is set out in D. Stairs, "Foreign Policy Consultations in a Globalizing World," in *Policy Matters*, Vol. 1, No. 8, Montreal: Institute for Research on Public Policy, December 2000.

[17] One senses that part of the impetus that is currently behind the discussion of the precautionary principle in fact derives from the at least tacitly acknowledged failures in managing the global commons.

How to Proceed – And What Lies in Store: The Road Map Looking Ahead

Given the circumstances, the central question is how best to engage new actors in our various countries in a creative and positive way while keeping in clear view the ultimate objective of more effective and enduring trade policies to achieve more sustainable economic growth.

First, it would seem appropriate and indeed necessary that governments get to know CSOs somewhat better. This will be no mean feat, given their proliferation.[18] In addressing this issue, Sylvia Ostry suggests that there are three broad functional categories of CSO coalitions or networks: "mobilization networks," whose chief objective is to rally support for a specific set of activities;[19] "technical networks" designed to provide information to CSOs to facilitate their participation in the policy process;[20] and networks dedicated to servicing developing countries, which she has dubbed a "virtual secretariat" for the latter.[21] Even this brief review underscores the need to approach CSOs on a rather more nuanced basis than has been the case to date. It also underscores the enormity of the challenge.

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[18] As Robert Keohane and Joseph Nye point out, "In the last decade of the 20th century, the number of international NGOs grew from 6,000 to 26,000, ranging in size from the Worldwide Fund for Nature with 5 million members to tiny network organizations." These figures exclude national organizations, underscoring the numbers issue. See R. Keohane and J. Nye, "The Club Model of Multilateral Cooperation and the WTO: Problems of Democratic Legitimacy," op. cit.

[19] In this category, Ostry includes organizations such as Ralph Nader's Public Citizen and Global Trade Watch; the U.S.-based Preamble Center; the U.K.-based Friends of the Earth, the Direct Action Network (DAN), the Ruckus Society, and Turning Point, an organization formed recently to produce advertisements on the effects of globalization on the environment. See S. Ostry, "The Uruguay Round North-South Grand Bargain: Implications for Future Negotiations," paper presented at the conference *The Political Economy of International Trade Law,* University of Minnesota Law School, September 15-16, 2000.

[20] In this category, Ostry includes the Centre for International Environmental Law in Geneva and Washington; the International Institute for Sustainable Development in Winnipeg; the Institute for Agriculture and Trade Policy in Minneapolis; the International Centre for Trade and Sustainable Development in Geneva; WEED (World Economy, Ecology and Development)

Secondly, in engaging CSOs, three solutions appear to suggest themselves: improved transparency, more and better analysis, and more inclusive consultations. All will necessitate a fundamental change in attitude on the part of governments, at both political and official levels. These ideas are taken up in turn below.

The case for transparency

With respect to transparency, it is clear that the entire system must be more open. Secrecy in our current socio-economic environment serves no one; it risks alienating everyone. For one thing, a lack of transparency breeds suspicion and cultivates an aura of exclusivity that is directly antithetical to democratic sensibilities. Secrecy is

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in Bonn; and the Institute for Global Communications in Palo Alto, California. These institutions, which are for the most part focussed on environmental and legal issues, provide technical and strategic information in support of CSO participation in the policy process, with the objective of influencing policy mainly by operating through institutional channels. Ibid.

[21] In this category, Ostry includes the Malaysian-based Third World Network and the Geneva-based South Centre (which collaborate to promote "south" solidarity on policy issues); SEATINI (Southern and East African Trade and Information and Negotiations Initiative), which obtains funding from UNDP and UNCTAD and seeks to build the knowledge base and capabilities of African countries; Focus on the Global South in Thailand, which seeks to link grassroots CSOs working on development issues; the Indian-based CUTS (Consumer Unity and Trust Society), which focusses on trade and sustainable development; the French-based Rongead, which obtains funding from the European Commission and the French government as well as private sources for its work on agriculture, trade and sustainable development; the Oxford-based Intrac (International NGO Research Centre), which trains and consults on behalf of developing-country CSOs; and a number of traditional development CSOs such as Oxfam and Christian Aid. Op. cit.

resisted on principle in democracies because the public does not know what it hides – indeed, it invites the inference that it shelters from scrutiny power broking that trades off interests of some against benefits for others without adequate compensation.[22] The reality is, of course, that genuine power broking is rarely done in formal terms;[23] accordingly, if secrecy of formal proceedings shields anything from public awareness, it is most likely the lame arguments, lackadaisical involvement, long-windedness and rhetorical posturing that all too often are inflicted on those engaged in international discussions.

More fundamentally, secrecy in negotiations and administration undermines the very possibility of full accountability and, in a not unrelated matter, tends to reverse the benefits that flow from consultations – indeed, it may well give rise to cynicism as to whether consultation is to inform public policy or is simply undertaken to mollify public opinion. Accordingly, allowing more sunshine into the WTO would not only be good for the organization itself but would also remove some of the fuel that feeds the public demonstrations against it.

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[22] This point also can be made in respect of the relationships amongst the members of the WTO itself, as was shown at Seattle by the adverse reaction to the proposal that emerged from the "green room" process by those WTO members not part of the group (the "green room" process consists of an informal consultative group within the WTO that tries to forge the basis for compromise amongst the larger trading economies as a precursor to proposals being put to the full membership). This issue is dubbed "I-transparency," or internal transparency in Geneva jargon, to distinguish it from "E-transparency," or external transparency, which is vis-à-vis non-members. For a discussion of the I-transparency issue, see S. Ostry, "The Uruguay Round North-South Grand Bargain: Implications for Future Negotiations," op. cit.

[23] For example, the forward movement in the Uruguay Round negotiations was to an important extent due to discussions in various small groups named after the restaurants in which they met, a point noted ruefully by those who ate their way through the Uruguay Round and have the waistlines to prove it. Nor, might it be said, is there anything untoward in this. Informal processes are no more foreign to intergovernmental affairs than golf-course deals are to business or brown-bag lunch discussions to CSO opinion generation.

CSOs have a well-established role in a national context as monitors of public policy implementation who use the media to hold governments accountable for honouring their commitments. The extension of this role to the WTO is perfectly natural and should be accommodated and facilitated insofar as is possible. At the same time, this would not resolve all issues: those most suspicious would conclude that transparency in the formal proceedings of the WTO would simply shift the "real" decision making to other, less well-lit venues.

How much transparency governments worldwide would be willing to allow into the WTO is an open question. Steps to promote distribution of documents, to place more official information on websites, and to facilitate and encourage more debriefings are necessary at a minimum.

The case for improved analysis

While the "democratic deficit" in the WTO, and the system of global governance more generally, was much discussed post-Seattle, the "analytical deficit" did not get as much attention. Yet arguably the lack of a compelling case for a new round was perhaps as much a factor in the ultimate demise of the Seattle Ministerial as any other. It should be noted that there are two facets to this argument: one is that the WTO members themselves were not convinced that the potential net benefits of a new round were too great to pass up; the second is that key constituencies such as business, as well as the general public, were equally unconvinced and thus did not provide the political support for the difficult decisions that ministers would inevitably have to make in "sensitive sectors." The analytical deficit thus reflects failure on both counts.[24]

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[24] The inadequacy of the analytical case supporting a new round of multilateral negotiations is detailed in Dan Ciuriak, "The 'Trade and...' Agenda: Are We at a Crossroads?" *Trade Policy Research 2001,* Department of Foreign Affairs and International Trade, 2001. This study shows that estimated gains

Arming the trade policy community with a compelling case for further liberalization is thus a clear analytical priority issue. Over and above what it would mean for ministers, improved analysis would serve to inform more meaningful communications efforts by governments and the pro-trade lobby more generally.

The weakness of the government message has been labelled a "communications deficit." It has been argued that this deficit reflects the primacy of economic variables such as "trade" and "growth" over the ultimate objective of growth and improved well-being.[25]

This particular weakness in communications is not unrelated to several other unfortunate tendencies in modern economic dialogue, including the primacy given exports over imports in trade policy communications: exports are of course the basis for jobs but, in economic terms, a country exports in order to obtain the foreign earnings to import. Imports are the real objective of trade, yet this point is rarely made in "selling" trade liberalization.[26]

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from a new round are considerable in gross terms, but the case for gains net of adjustment and other costs, including opportunity costs of pursuing alternative policy initiatives (e.g. technology dissemination) has simply not been made. Finally, while it was generally recognized that the key to the new round was a good offer (including market access and technical support) to the developing countries least integrated into the multilateral system, the adequacy of the package was never convincingly demonstrated.

[25] This observation is due to my colleague David Lee at the Department of Foreign Affairs and International Trade. He emphasizes that it is not enough to assert an indirect (e.g. "trickle down") benefit; rather, the detailed "working through" of the linkages and the handling of trade-offs need to be laid out for the dialogue to be meaningful to today's discussants.

[26] This point is developed in a study on the benefits of imports currently being developed by Clea Coronel of the Department of Foreign Affairs and International Trade. A second example, which is of tangential relevance here, is the triumph of national accounting language over common sense in everyday discourse. This has resulted in the arid accounting category of "consumption" turned into the idea of people being "consumers." In turn, this has led to the portrayal of all that individuals (or households) do as "consumption," whether it be enjoyment of the fresh air in a natural park (paid for by a ticket at the

One area in particular where governments, as well as non-governmental experts, will have to be more responsive is with regard to the expressions of uncertainty or of fear from the general public concerning the impact of liberalization: these uncertainties and fears should be faced head-on with facts and analysis; they cannot be dismissed as overreactions of the un- or ill-informed.[27]

Part of the burden of improved analysis needs to be shouldered by the WTO itself, both through expanded in-house research activity and through development of its own networks with academic and non-governmental think tanks and organizations. While the WTO Secretariat should not adopt an advocacy posture – that role should be assumed by the Director-General and the members themselves – it needs to be, and to be seen as, an authoritative voice on the issues themselves. The work of the

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entrance), the viewing of a work of art (paid for by the price of admission to the museum or art gallery) or the obtaining of essential medical care (paid by medicare if one is fortunate enough to be Canadian). Labelled "consumption," such activities get lumped in with everything from gluttonous overeating to excessive use of gasoline from driving gas-guzzling SUVs to the corner store for milk. This allows the short and easily made intellectual leap from "consumption" to "excess consumption" by those who question the objective of growth with no more apparent ultimate purpose than to have more clothes than closet space or more cars than the roads can accommodate. By the same token, the expenditure on gasoline required to sit for an hour in rush-hour traffic, and the purchase of medicine to alleviate lung problems caused by breathing poisonous exhaust from other cars in the process, because infrastructure development has not kept pace with growth, are also considered "consumption." In the developed countries (especially during economic booms), the equation "more growth = greater welfare" cannot always be directly made; the "communications deficit" derives from the failure to internalize this.

[27] These concerns are many and varied, ranging from the impact of trade liberalization on social contracts and on the fabric of societies to the role of trade in truly fundamental issues such as global warming and biodiversity. These concerns generally fall under the rubric of "trade and …", an issue area that is only starting to receive the in-depth rigorous analysis and policy attention that it deserves. For an overview, see Dan Ciuriak, "The 'Trade and…' Agenda: Are We at a Crossroads?", op. cit.

Secretariat should feed into the policy debate and, by the same token, open up channels for participation by outside experts in an intellectual capacity. Some ideas have been advanced as to how this might be done and what it would mean for the WTO.[28]

The case for improved consultations

Finally, governments, international institutions and non-governmental experts must not carry on trade policy discussions over the heads of the general population. More and more effort will have to be directed to building a consensus on issues affecting individuals directly, both in developed and in developing countries. In the national context, in Canada for example, public notices through the *Canada Gazette,* legislative hearings, ongoing private sector consultations or multi-stakeholder consultations, a more current, complete, user-friendly website as well as polling all can be used to help develop a consensus around national trade policy interests and objectives.

This consensus building can also be done in the WTO context, for example, by holding more high-level meetings on specific difficult issues, as was done in March 1999; wider distribution of documents will also help. However, the key issue revolves around a more direct involvement of CSOs in the work of the WTO.

In this regard, attention has centred on the acceptance by WTO panels and the Appellate Body of amicus curiae ("friends of the court") briefs in disputes. Amicus briefs have been admitted in several WTO cases:

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[28] For example, Sylvia Ostry has proposed restoring to the WTO a body for policy discussion, which it has gone without since the suspension in 1990 of the Consultative Group of Eighteen (CG18): "In the terminology of the international regime literature the policy forum could become a broad meta-regime founded on mutually agreed basic principles and fostered by a combination of strategic assets: a knowledge infrastructure in the form of a research capability; a meeting infrastructure for knowledge diffusion, debate, peer group pressure; strategic planning and monitoring of policy performance." See S. Ostry, "WTO: Institutional Design for Better Governance," op. cit.

- *United States – Shrimp Turtle:* In this highly controversial 1998 decision, the Appellate Body ruled that panels had the right to accept unsolicited information from non-governmental sources, and to accord it whatever weight was appropriate. The Appellate Body noted that Dispute Settlement Understanding (DSU) Article 13 allowed panels to "seek information," and concluded that this provided panels with the discretionary authority to accept and consider any information or advice submitted to them, whether requested or not.
- *United States – British Steel:* In this May 2000 decision, the Appellate Body determined that it too had the authority to receive and consider amicus briefs from non-governmental sources, where it found it "pertinent and useful to do so." The Appellate Body based this on the broad authority given it by the DSU to adopt procedural rules.
- On November 7, 2000, the Appellate Body Division decided, in the context of Canada's appeal of a decision upholding a French ban on asbestos imports in the *Canada – Asbestos* case, to establish a procedure to allow CSOs and others to seek to submit amicus briefs to the Appellate Body.

These actions by the WTO's Dispute Settlement Body (DSB) were warmly welcomed within the CSO community, which interpreted them as acknowledging the importance of civil society participation and the value that such participation could bring to the process. By the same token, these actions were highly controversial within the WTO membership; indeed, a special meeting of the WTO General Council was convened to review the procedure that the Appellate Body had established to allow CSOs to request permission to submit briefs.

That the DSB was "pushing the envelope" with these moves, and especially the latter two, is fairly clear, as they represented decisions on matters that had been considered, but not agreed to, during the Review of the Dispute Settlement Understanding in 1998-1999. In particular, during the DSU Review, proposals had been made to:

- expand the Appellate Body's scope of review to allow it, under certain circumstances, to review "manifestly erroneous or unreasonable characterization or appreciation of the facts before a panel"; and
- deal with unsolicited information from outside sources.[29]

Amicus briefs would for the most part deal with facts and their interpretation rather than the interpretation of WTO provisions; accordingly, insofar as the Appellate Body restricts its scope of deliberation to interpretation of WTO law (which is where the failure of the members to amend the DSU in line with the proposal to expand the Appellate Body's scope of review left matters), the point of it receiving amicus briefs is unclear.

Similarly, the decision to establish procedures to accept unsolicited briefs represented a decision on a matter considered but left unresolved by WTO members during the DSU Review.[30] Further, it appears to create procedural inconsistencies in connection with two other proposals considered but not agreed to in the DSU Review:

- to open Appellate Body hearings to the public; and
- to allow WTO members that had not been third parties before a panel to appear before the Appellate Body on appeal.[31]

Insofar as those submitting amicus briefs might be invited to explain issues to the Appellate Body, members of the public would be allowed into Appellate Body hearings. Moreover, unless other WTO members were given the same right, they would appear to be less privileged than CSOs.

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[29] See Debra P. Steger, "The Appellate Body and Its Contribution to WTO Dispute Settlement," paper submitted to the conference *The Political Economy of International Trade Law,* University of Minnesota Law School, September 15-16, 2000.

[30] A similar proposal had also been put forward unsuccessfully during the Uruguay Round.

[31] See Debra P. Steger, op. cit.

How this issue will play itself out is unclear. The decision of the WTO *not* to accept briefs in the *Canada – Asbestos* case after several environmental CSOs and at least one academic requested permission to do so was interpreted by some CSOs as a clear sign of failure to "learn the lessons from Seattle."[32] Accordingly, there is more than a little public relations fallout from this for an organization that is sorely in need of better public relations. More importantly, the Appellate Body *has* dealt with substantive issues – and probably must continue to do so if it is to fulfil the broad purpose envisaged for it, namely of serving as a safeguard against bad panel decisions.[33]

Whatever the course ultimately charted by the WTO, governments and international institutions will have to make an attempt to engage constructively with as many non-government groups as possible. While experience shows that some of these groups will be reluctant and/or hostile, most CSOs will respond with interest and with positive ideas. The alternative is to be continually on the defensive, fending off criticism from both these groups and the media, which will often result in a waste of effort and of momentum.

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[32] See "A Court without Friends? One Year after Seattle the WTO Slams the Door on NGOs," press release issued by Greenpeace International et al., November 22, 2000.

[33] The technical complexity of issues considered by the Appellate Body under the SPS Agreement – such as the Beef Hormones and Australian Salmon cases – provides some justification for procedural flexibility to admit expert witnesses. For a discussion of this issue, see M. Trebilcock and J. Soloway, "International Trade Policy and Domestic Food Safety Regulation: The Case for Substantial Deference by the WTO Dispute Settlement Body under the SPS Agreement," paper presented at the conference *The Political Economy of International Trade Law*, University of Minnesota Law School, September 15-16, 2000.

And, perhaps uncomfortably for those within the trade policy community, the possibility that policy may change due to the consultations must also be countenanced – and that trade rules may at times have to defer to other imperatives.[34]

Some Tentative Conclusions

Overall, given the information revolution and the evolution of a more democratic means of policy formulation in many countries around the world, increased involvement of CSOs will be a fact. And there will be difficulties: the rough and tumble tactics of some CSOs will not be comfortable for some politicians and particularly for their officials; expectations might be raised by the very fact of consultations that no government will be able to meet; and the process of negotiations might well be slowed down because of the need for, or expectation of, consultations.

Moreover, given the complexity and inexact nature of the social sciences, uncertainty about the appropriate policy to adopt in a given situation will never be entirely removed. In such circumstances, governments must lead, notwithstanding the fact that not all will agree. But equally clearly, it is best if governments lead after having benefited from a comprehensive debate in which all views are put on the table.[35]

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[34] Michael Trebilcock and Julie Soloway make the case for "substantial deference" of WTO rules in certain cases. See M. Trebilcock and J. Soloway, op. cit. Dan Ciuriak generalizes this idea to instances where vital interests and social values are at play. See D. Ciuriak, "The 'Trade and...' Agenda: Are We at a Crossroads?" op. cit.

[35] A comment from Steve Charnovitz, a noted environmental lawyer, underscores this point most aptly: "Just as national democracy entails participation and debate at the domestic level, so too does democratic global governance entail participation by transnational NGOs. Politicians should act and decide as a result of listening to a vigorous debate. It is illusionary to think that governance can be improved by having the decisionmakers of today rule out options for the people of the future."

The advantages, particularly in the longer term, are many: public buy-in will be deeper and longer lasting, the substance of trade negotiations will be strengthened, and social cohesion in our various nation-states will be enhanced – all key to effective public policy and to the general betterment of society.

"Most WTO governments oppose NGO participation on the grounds that the WTO is an exclusive club of States/governments. Although this view of the WTO is certainly accurate on one level, it misses the possibility of a fuller conception of the WTO and its constituents. The recent WTO Section 301 panel, perhaps recognizing the hollowness in conventional images of the WTO, called our attention to the needs of individual traders. According to the panel, the multilateral trading system is 'composed not only of States but also, indeed mostly, of individual economic operators' (para. 7.76). One might doubt that the panel accurately states the international economic law of today, but I predict that they postulate the international law of tomorrow." See S. Charnovitz, "On Constitutionalizing the WTO: A Comment on Howse and Nicolaidis," discussants' comments delivered at the conference *Efficiency, Equity and Legitimacy: The Multilateral Trading System at the Millennium*, Center for Business and Government, Harvard University (www.ksg.harvard.edu/cbg/trade).